DIESEL FUEL EXCISE TAX COLLECTION PROCESS

HEARING

BEFORE THE

SUBCOMMITTEE ON ENERGY AND AGRICULTURE

OF THE

COMMITTEE ON SMALL BUSINESS
HOUSE OF REPRESENTATIVES

ONE HUNDREDTH CONGRESS

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DIESEL FUEL EXCISE TAX COLLECTION PROCESS

THURSDAY, MARCH 3, 1988

HOUSE OF REPRESENTATIVES,
SUBCOMMITTEE ON ENERGY AND AGRICULTURE,
COMMITTEE ON SMALL BUSINESS,
Washington, DC.

The subcommittee met, pursuant to notice, at 10 a.m., in room 2359-A, Rayburn House Office Building, Hon. Charles Hatcher (chairman of the subcommittee) presiding.

Present: Chairman Hatcher; Representatives Ray, Martinez, Dreier, and Combest.

Chairman HATCHER. Good morning. I am Charles Hatcher, chairman of the Subcommittee on Energy and Agriculture of the Small Business Committee. I thank you for your interest as evidenced by your being here for the hearing.

First, I would like to thank Larry Combest for taking the lead in addressing this issue that is important to many of us and many of the people we represent in rural America.

I will keep my opening remarks brief in the interest of time, because we have quite a list of witnesses here, today. I would also like to take this opportunity to ask you to be as brief as you can. Any written statements that you have provided will be entered into the record in their entirety.

Today, we plan to review not only H.R. 3865 which is the bill introduced by Mr. Combest and many others of us, but the entire question of this diesel fuel excise tax collection process. It has certainly sparked some interest across rural America and in the Congress. We have 11 House bills already and 4 Senate bills addressing the issue. I regret that we do not have a representative from the Internal Revenue Service here today, because I have some questions of them on how they plan to address the subject if we do not get legislative change before April 1. I was disappointed that they refused to be here, today. But I, along with other members of this subcommittee, will send a list of questions to Commissioner Lawrence Gibbs of the Internal Revenue Service that we feel would have been asked of him had he been able to appear before us today.

[The questions and the Internal Revenue Service's response with their prepared statement may be found in the appendix.]

Chairman HATCHER. This issue appears to be a good example of an action taken by Congress in the context of a large bill without really examining or being aware of the consequences of what that

action is going to be on many small businesses and farmers throughout the country.

If the proposal goes through on April 1 without delay by the IRS or without some legislative change, it is really going to wreak havoc on many farmers and small business people who can ill afford to pay that tax and then wait to get a refund or some tax credit later.

Therefore, it is the purpose of this hearing to give you the first opportunity to express yourselves about the burden that this may place on folks such as that, and I hope we are able to develop a record here today that will help us in moving legislation and getting some response from the IRS.

At this time, I would like to recognize the ranking minority member, Mr. David Dreier, for any comment he may have.

[Chairman Hatcher's opening statement may be found in the appendix.]

Mr. DREIER. Thank you very much, Mr. Chairman. I congratulate you for calling this hearing and while I am one who has always heeded that old adage, "Don't throw the baby out with the bath water," I have to say that today's hearing is clear evidence to me that I am very proud to have cast a "No" vote when the Budget Reconciliation bill came before us at the end of last year. I continue to be amazed at the number of hoops that our farmers and small business people are required to jump through in order to comply with the very burdensome tax which exists, and, as we approach April 15, we know how that burden is being felt.

The new procedure for collecting diesel fuel excise taxes will create an administrative nightmare and financial hardships for both farmers and small business people. Our farmers, alone, will have to pay $450 million in reimbursable taxes this year unless the law is changed. To pay the tax and file for a refund, they must spend more hours away from income-producing activity or hire new employees to comply with the increased administrative burden.

I understand that the purpose of this new law is to help lessen the auditing burden on the Internal Revenue Service. As far as I am concerned, it is more important that we ease the stifling tax burden on our farmers and small business people. They need money to buy seed and equipment, not to help ease the tax collection burden of the Internal Revenue Service. If it was not for these small firms, there would be few taxes for the Internal Revenue Service to collect. This provision just does not make sense, Mr. Chairman.

I am very proud to be a cosponsor of H.R. 3865, which was introduced by our friend and colleague, Mr. Combest of Texas. It would restore the diesel fuel excise tax exemption for offroad vehicles. I support strongly the Combest bill because it is not just limited to farmers, but includes other enterprises which rely on offroad vehicles for their livelihood.

Mr. Chairman, again, you are to be commended for recognizing the seriousness of this problem. We have a very distinguished group of witnesses, many of whom are colleagues of ours. I only want to add that I am very disappointed, along with you, Mr. Chairman, that the Internal Revenue Service could not come to defend the need for this onerous new tax collection procedure.

I look forward to working with you and my colleagues on the panel, and I hope very much that we will be able to restore the diesel fuel tax exemption for offroad vehicles. Thank you very much, Mr. Chairman.

Chairman HATCHER. Next, Mr. Ray for any comments.

Mr. RAY. Thank you, Mr. Chairman. I do want to align my remarks with those of my colleague, Mr. Dreier, and with yours. Let me say at the outset, we are very busy in the Congress right now. I think I am on three committees that are meeting right now at the same time, but this is the first in priority. I wanted to be here to make a statement to recognize the people who are here. But I will have to leave shortly after I make this statement.

Mr. Chairman, I want to thank you for holding this hearing today. The change in the collection point on the diesel fuel tax will cause a great hardship on farmers, and wholesale petroleum distributors, and builders, and contractors, and others. I believe it is important that this matter be thoroughly examined by the Congress.

Mr. Chairman, this is really just a further example of antibusiness and agricultural legislation that we in the Congress who are advocates of trying to make this fragile economy work have to battle over and over.

Such things as parental leave, prenotification, an increase in minimum wage, mandatory health care, a host of other items, legislative items and regulations which simply drain away the profits that we have in our businesses and in our agriculture.

I would like to just take a minute to say that we are in pretty bad shape in this country right now. The last 9½ years we have driven up our national debt to the point where the interest alone in 1988 is the second largest item in our budget. It is about 17.5 percent of the budget, $173 billion, and, as we try to correct these things, we have to keep this fragile economy and the business industry alive and well, because if we do not do it, we will drive the country into a downturn, a recession, and there will be less money coming into the Treasury and more people unemployed.

So, I think it is very important that we attack such things as this paperwork burden, this financial burden that is being placed by this particular regulation. I would make note at this time, also, that the Ways and Means Committee turns their staff loose and asks them to go out and find $10 or $15 billion. They find all of these things, and, all of a sudden, they crop up in the legislation, and they tend to get worse as the time goes on. So, we have to deal with it as harshly as we can.

I am pleased also, today, that a constituent of mine, Mr. Jim Reid is here today to give testimony on this issue. Mr. Reid owns and operates a 1,700-acre farm in Sumter County, GA. He was the 1985 American Farm Bureau National Young Farmer of the Year, and he has also served on the State board of directors for the Georgia Farm Bureau. I know that we will benefit from this young man's testimony later this morning.

Also, accompanying him in our audience is Mr. Bob Nash, president of the Georgia Farm Bureau attesting to the seriousness that he sees in this particular regulation which is creating this problem.

Today, we are here to examine H.R. 3865 which was introduced by my colleague and fellow committee member, Larry Combest. I am an original cosponsor of this legislation. I want to commend Congressman Combest for his leadership on this issue. H.R. 3865 would permit the tax-free sales of diesel fuel for use on a farm or other offhighway uses such as construction. Unless this bill or similar legislation passes soon, farmers and contractors who buy diesel fuel from wholesalers will begin paying the fuel tax on April 1, 1988. Later, the farmer or the construction company will be able and have to apply for a refund for the fuel which was for offhighway purposes and uses.

To me, this is similar to that rule that IRS came out with saying that you have to record your mileage from point to point. We were successful in killing that and turning it over, and I believe we are going to be able to do the same here. We hope so.

I believe it is unfair and inefficient for the Federal Government to collect a tax and then refund it. All this does is to tie up capital for a period of time without any payment of interest or other compensation plus the unknown cost of the paperwork burden, itself, on the Government. In my opinion, farmers and contractors that do not owe this tax should not be required to pay it.

I have written Congressman Dan Rostenkowski, chairman of the Ways and Means Committee, and encouraged him to address this situation. To date, the Ways and Means Committee has not taken any action. I am hopeful that this hearing today will increase the awareness of Members to the importance of this issue.

Mr. Chairman, I commend you for holding this hearing today, and I am grateful for the opportunity to come and testify.

Chairman HATCHER. Thank you.

Next, I recognize Mr. Combest for an opening statement.

Mr. COMBEST. Mr. Chairman, I want to begin by commending you for the speed with which you called this hearing. This issue is truly one that has come to Congress from the very grassroots of this country. We have heard an overwhelming cry from farmers, from oil field drillers, from tugboat operators, and from contractors to change this law. I am particularly pleased to welcome my chairman of the Agriculture Committee, Mr. de la Garza, and my Senator from Texas, Mr. Gramm to both testify on this legislation.

I introduced H.R. 3865 on January 27 to prevent all offroad users of diesel fuel from paying a tax which they do not owe. Since that time, more than 90—in fact, today, 93 of my colleagues have joined me as cosponsors, and the Texas Farm Bureau, the Permian Basin Petroleum Association, and dozens of other national organizations have endorsed my proposal. The message is coming across loud and clear: Our constituents demand action.

The newly enacted tax, which would take effect on April 1 just does not make any sense. It will require additional upfront capital from small businesses, from farmers, those least able to afford it. The Internal Revenue Service's use of their money will create a cash-flow burden and an unnecessary interest expense on industries which are already experiencing serious economic troubles.

Oil field drillers, farmers, shrimpers, and builders have a hard time understanding the logic of a law which requires them to pay a tax they do not owe, prove to the Government that they do not owe

it, then apply to the Government for a refund they will hopefully be paid. All this, for a tax we have established should not have been paid for in the first place.

In addition, the new law causes serious cash-flow problems for industries that are least able to stand it. The collection point change requires that oil drillers and farmers in my district allow IRS to use their money, interest free, because the agency is doing a poor job of administering present regulation. To explain the serious financial implications of this law and why it is just bad policy, let me share just a few samples of letters I have received from our constituents, and I could add many more.

From the Sitton Drilling Co. in Lubbock: The Sitton Drilling Co. operates five drilling rigs which average 500 gallons of diesel fuel per day per rig, or a total of 2,500 gallons per day. This additional tax will cost a total of $377.50 per day, $11,325 per month, $137,787.50 per year.

Lewis Block, who is a farmer, says, "This tax will result in my having to borrow an additional $2,200 just to pay the stupid tax. It is hard enough to borrow money these days without having to put up with this."

Yale Key, of Oil Well Services says, "We have bought fuel tax exempt for years and pay the Federal tax quarterly on the amount used on public highways. Sixty percent of the average 50,000 gallons we buy each month is exempt. It will cost us $4,530 a month."

The IRS wants our constituents to do their job for them. Because they are incapable of enforcing their own collection policy, they are going to ask all users of diesel fuel, liable for the excise tax or not, to police the collection process for them. I believe the Congress wants to make sure that those evading the tax are caught, and I think the Members have expressed their willingness to look into alternative ways to proceed.

On the other hand, my colleagues and I will not stand for a policy which assumes users of offroad diesel fuel are guilty of evasion until the IRS decides they are innocent.

I fully agree with the agency that a need for an improved collection mechanism exists. I further understand that Internal Revenue Service has not been able to collect all excise taxes owed to the trust fund. While my record of support for the Highway Trust Fund speaks for itself, funding for maintenance and safety of our public roadways is not the issue in this debate.

I want to welcome S.M. True, who resides in my district, and who is president of the Texas Farm Bureau. His organization has done a tremendous job bringing this issue into focus and assisting many of us here in our efforts to inform other Members of the serious problems associated with this policy. Also from Texas, and here at my request, Harry Spannaus, of the Permian Basin Petroleum Association, will explain the specific problems that the new law creates for the energy industry.

Let me add this final thought. It is particularly appropriate for the Small Business Committee to be the first to hold hearings on this issue. For multimillion dollar corporations, an extra 15 cents a gallon for diesel fuel will not matter that much. But, it could mean the crucial difference for many of our small businesses in my district and throughout the Nation. Many small businessmen and

farmers will be the ones to feel the pinch if we do not find a workable answer. I look forward to working with all of my colleagues to see that we can make something happen. I appreciate their support for this bill. Thank you, Mr. Chairman.

[Mr. Combest's opening statement may be found in the appendix.]

Chairman HATCHER. Thank you.

Our first witness this morning is Chairman Kika de la Garza, chairman of the House Agriculture Committee. We welcome you, Kika, at this time.

TESTIMONY OF HON. E. (KIKA) DE LA GARZA, A REPRESENTATIVE IN CONGRESS FROM THE STATE OF TEXAS

Mr. DE LA GARZA. Mr. Chairman and members, your opening statements have well documented the problem, and I will submit my statement for the record. Just let me say that this is a very important issue as far as agriculture is concerned. But not only for agriculture, but also for the oil and gas industry, the fishing industry, the construction industry, all of which are suffering, to say the least, at this time, and your hearing is very timely. In order to bolster the support for the legislation, I also will call hearings in the Agriculture Committee so that we might impress on our colleagues from the Ways and Means Committee who have the jurisdiction over this issue that we are very supportive of the various bills.

Let me add that I was working on this legislation and unbeknownst to me, other members were also, so, we wound up with many bills. Though I would say probably more my fault than my staff's, we wound up introducing the same bill as Mr. Combest, all in the desire to do something. But I would yield to any of the bills, as I have so stated to the Ways and Means Committee. Who the author is, is not as important as getting the jobs done for our farmers, and our oil industry, and the construction industry.

Let me just give you, briefly, one example. We had a call this morning from Aycock Oil Co. located in Alice in my congressional district. This company basically sells diesel fuel to the oil industry. Mr. Aycock may sell to a drilling rig or rigs as much as 100,000 gallons of diesel fuel a month which means that he, as the wholesaler, will have to carry the tax on his books and collect it from the drilling rig operators. This would put a tremendous burden on him. It would put a tremendous burden on the rig operators plus all of the ensuing paperwork that is now a burden, at best, at this point, without this onerous regulation.

So, I thank you for having this hearing to further bolster the legislation when it might be considered by the Ways and Means Committee. I thank you.

[Mr. de la Garza's prepared statement may be found in the appendix.]

Chairman HATCHER. Well, thank you for being here, Mr. Chairman.

Does anybody have a question?

Mr. DREIER. Mr. Chairman, I would just like to comment briefly on your testimony and congratulate you for introducing identical legislation. I remember back in 1982 when we were attempting to

repeal that 10-percent withholding on interest and dividends which had been in the midst of TEFRA. There were 180-some odd identical bills introduced to do the exact same thing, to repeal it. Maybe, while everyone, of course, has joined in cosponsoring Mr. Combest's bill, a litany of identical pieces of legislation just may help accomplish the goal.

Mr. DE LA GARZA. I thank you, Mr. Dreier. The more Members or as many more Members as we can get behind us, I think would impress our colleagues on the other committee.

Chairman HATCHER. We appreciate your being here this morning, Mr. Chairman. Thank you.

Mr. DE LA GARZA. Thank you very much, Mr. Chairman.

Chairman HATCHER. Has Senator Gramm arrived?

If not, we will call those whom we have identified as panel 3, who are four Members of the House, Ms. Schneider, Mr. Schuette, Mr. Daub, and Mr. Jontz. Unless you gentlemen have some other preference, we will hear from you in the order in which I called you. Is that in agreement? OK. Mr. Schuette.

TESTIMONY OF HON. BILL SCHUETTE, A REPRESENTATIVE IN CONGRESS FROM THE STATE OF MICHIGAN

Mr. SCHUETTE. Thank you very much, Mr. Chairman, and my colleagues. Good morning.

I appreciate the opportunity to speak on this important issue facing Congress today. For my part of this discussion, I would like to focus on agriculture and how we should remove the needless tax burdens from the backs of our Nation's farmers and their families.

To collect the highway fuel taxes from offroad users is unfair. I commend the subcommittee, and particularly my friend and colleague, Mr. Combest, for their attention to this matter.

Before I begin, I want to add my name to those who strongly support the legislation of my friend and colleague from Texas. We need to insure that our farmers and their families, indeed, all offroad users, are provided with much needed relief from paying taxes that they simply do not owe.

While the case in point here, today, is the diesel tax, I would like to discuss a bill that I have introduced, H.R. 4007, which deals with both the gas and the diesel tax as it currently affects farmers.

Under the current law, farmers are exempt from paying the 15-cent-per-gallon highway tax on gasoline and diesel fuel used on the farm. However, because the 1986 Tax Reform Act changed the point of tax collection up the line closer to the refinery and away from the farm, farmers now have to prepay tax on their gasoline purchases. Farmers can file for refunds, but only after they have prepaid substantial sums of money which they do not owe.

Then, as if to make a bad policy worse, Congress passed the Budget Reconciliation bill last December and added diesel fuel to this unfair mechanism. Now, beginning on April 1, farmers will have to prepay the 15-cents-per-gallon highway tax on diesel fuels for—and let me remind my colleagues once again—taxes they have no obligation to pay.

Like the gasoline precedent, they must pay a tax and then file for a refund either at the end of the year or when they prepay

more than $1,000. That is why I have introduced H.R. 4007, a bill calling for the elimination of the fuel tax which would allow farmers to file for an exemption with the IRS for both the gas and the diesel tax. If this law is not changed, most of the money that farmers will have to pay to the IRS will be money that farmers would otherwise use to plant their crops. Because it is money that will be refunded to them only after the year is ended and after the damage is done, the current arrangement amounts to farmers giving the Federal Government, in essence, an interest-free loan. A loan that many farmers will have to borrow to afford. A loan which is unfair and is the worst nightmare for already over-burdened farmers and their families.

My bill would remove this exemption and still protect against any possibility of noncompliance or fraud which is the only justification for this change. Furthermore, it eliminates a lot of redtape and in the words of one farmer from my district, "... all the costs that are involved in refunding money that was theirs to begin with."

Now is not the time to put obstacles in the way of the recovery of rural America. Not only do I urge support of my colleague's bill, but I urge you to take a hard look at my bill, H.R. 4007 which calls for the elimination of not only the diesel tax, but also the gasoline tax as well. There is no reason that farmers should be unfairly burdened and forced to pay taxes they simply do not owe.

I hope all of my colleagues will work with me to pass this legislation into law. I thank you for your courtesy. My colleagues, I thank you.

Chairman HATCHER. Thank you for your testimony.

Mr. Dreier, do you have any questions? Mr. Martinez.

Mr. MARTINEZ. Yes. As I understand the problem, it is that farmers have to pay the excise tax up front and then file for an exemption to get their money back. I can see where that is nonsense. I mean it is really stupidity.

I am aware that the previous exemption system had a problem with exemption certificates being forged. But it seems that the natural response would be to provide certificates which cannot be counterfeited. There are plenty of ways to do that. Moreover, the counterfeit scheme will not work in most rural areas because their sellers of fuel do business with the same people all the time. They know who the farmers are that are using this diesel fuel or gas on their farms. That is not the problem.

By the same token, I am concerned that people who are not exempt, actually pay that diesel tax. If the exemption is simply stated as for "offroad use," then it may be too broad, especially if it includes recreational vehicles. I assure you that poor people do not have recreational vehicles, and the poor farmer does not necessarily have a recreational vehicle. He is more concerned about exempting from the excise tax the vehicle that he needs to do his work. That is what he is concerned about.

So, the issue is how do we exempt only those people who should not pay the tax. Exempting all offroad vehicles would be too broad because a lot of times these vehicles are used "onroad" to get to an offroad area. I might add that offroad vehicles can cause a lot of maintenance problems in offroad areas of publicly owned parks

and recreational areas; damage for which somebody has got to pay. How do we separate and define the two so that we do not let people who should pay the excise tax get away with not paying it?

Nobody wants the farmer who uses a vehicle on his farm—not using it on the road, not making any wear and tear on the road—to pay that tax. He should not have to. I agree.

But how about the others? How do we make that definition? How do we separate them?

Mr. SCHUETTE. Mr. Martinez, you may not have a farm constituency, but, sir, I think you have correctly put your finger on the issue here. I cannot completely justify or explain the rationale which pushed to make this change, bring it further up the line away from the farmer, away from the offroad user, because I think the rationale falls apart.

Part of it, as I am told, was a concern about fraud or those who were not entitled to not pay the tax might be taking advantage of the system, hence, that might be some motivation for changing it.

My bill, and others like it, would be dealing with agriculture use on gasoline and diesel so that you have an exemption you file with the IRS to try to eliminate any cause for fraud or unjust enrichment at the expense of the tax code. Other issues like this, similarly with the construction industry as well. But my bill would have farmers file for a one-time exemption, so that we have a specific close of any loophole or any abuse of the system.

Mr. MARTINEZ. Then your bill just provides exemption for those who really merit it.

Mr. SCHUETTE. Strictly to the farm family, the user, offroad use for farm vehicles; yes, sir.

Mr. DAUB. May I respond, Mr. Chairman? I have not testified yet, but the history of all of this comes out of a hearing 2 years ago where the IRS and other parties testified that there was a compliance problem principally aimed at construction industries and the use by certain elements of business in the New York City area with respect to purchases, and point of purchase, and the evasion of payment of tax on fuel that actually was used on the road but that was arguably not used on the road. From that came a serious compliance question by the IRS, and farmers and others were very unjustly, then, lumped into the thinking on this matter. It has progressed to the point now where it was tucked into the Trojan Horse of a reconciliation bill in December, and that is why we are all here today.

Chairman HATCHER. We need to do something about that.

Mr. MARTINEZ. Representative Daub, you bring up a good point. Why should farmers' offroad vehicles be held not responsible for the tax while another person in a different industry, such as construction, would have to pay the tax on his offroad vehicles? There are a lot of construction vehicles which are not used on the road but are instead transported to an offroad worksite by another vehicle that does use the road. That person should pay the tax on the vehicle which does use the road, but not on the vehicle he unloads. I will give you a good example. Tote motors, which are little mechanical lifts, are transported on another vehicle, but they, themselves, do not use the road. Why should they pay the tax?

Chairman HATCHER. If you ladies and gentlemen would not mind, Senator Gramm is here, and I would like him to come sit where you are, Mr. Schuette, if you do not mind, for a minute. Let him give his testimony and get back to the other side of the Capitol. How about that?

Mr. SCHUETTE. I am happy to do that, Mr. Chairman.

Chairman HATCHER. Phil, we welcome you here, today, and we look forward to your testimony.

TESTIMONY OF HON. PHIL GRAMM, A U.S. SENATOR FROM THE STATE OF TEXAS

Senator GRAMM. Mr. Chairman, let me thank you for giving me an opportunity to come and testify. We were in the midst of trying to finish a debate and have a vote, and I thought I could catch the vote before I got over here. But, unlike the House, the Senate has no rules so that while everybody had agreed to be brief, several Members obviously were caught in a moving speech. So, I figured I could dart over here, and do what I came to do, and get back.

I want to congratulate you for holding this hearing. I think there is a very real problem here. I think it is clear that when we acted on the Budget Reconciliation bill in the waning hours of the year and the session, that it was not fully understood what the impact of this was going to be.

The goal of trying to collect taxes is a worthy goal since Government is not free and, as we all know, very expensive. Some of us think too expensive.

The problem is that we have sort of an anomaly here where we are forcing people to pay taxes they do not owe. Then we are forcing them to keep this paper trail which is sort of like the provision we had before where people that use their automobiles for business purposes had to keep all these contemporaneous records.

Under the new diesel tax rules, if any diesel user pays more that $1,000 in diesel taxes in any quarter that they really don't owe, which will not include a lot of farmers and ranchers in my State, they can file on a quarterly basis and get their money back. If they do not pay that much in, they are going to have to let the Federal Government use their money for a whole year before filing for a refund.

In agriculture alone, we are looking at $426 million that farmers and ranchers in this country will pay to the Federal Government as a tax that is not owed. Then all those farmers and ranchers will be forced to keep all this paperwork to turn in at the end of the quarter or the end of the year to get their money back. During this time, the Federal Government would have had it interest free.

Additionally, I am a little bit concerned if the Government gets used to having it, maybe they will want to keep it.

The problem does not end in agriculture. You need to realize that in the Senate, I have introduced two bills that are roughly equivalent to the Combest bill. One bill is strictly for agriculture; the other bill deals with everything else—all of the heavy offroad users of diesel, including the shrimping industry, the oil industry, the construction industry, the maritime industry, and the inland

waterway users. All of these are users who will be paying a tax they do not owe.

We are only now beginning to get the feedback from all the grassroots organizations that are for it. Quite frankly, I think we have a good chance of seeing the tax repealed in the Senate. I think it will be very easy for us to come up with a procedure whereby exempt users can simply sign a form that can count against the wholesaler's tax that the wholesaler has to pay at the point of purchase where they are trying to collect. So, I think there is a fairly simple procedural solution. I think it is something that we should do, and I am hopeful that we can get it done.

I do not think there is any organized opposition to doing this. It is hard to get a budget figure on it, but I am not finding that there is any significant budget gain other than this interest-free money. So, I think this is a problem that should be fixed, and I commend this committee for looking at it. I want to pledge to you that there is a growing number of Members of the other body who are concerned about this and want to work with you to see that we get it done.

Chairman HATCHER. Well, that is good news, Senator. We are glad to hear there is that much interest in the Senate about moving some legislation. We appreciate that.

Mr. Dreier, do you have any questions?

Mr. DREIER. Thank you very much, Senator. I appreciate your coming all the way over here to our side to give us the benefit of your insight on this. I wonder if you could very briefly tell us what happened in those waning hours in the Senate as the debate on this diesel fuel tax came up?

Senator GRAMM. Well, people get old and tired in those waning hours.

Mr. DREIER. You certainly——

Senator GRAMM. Well, I never get old and tired.

Mr. DREIER. I know.

Senator GRAMM. It is easy for me to say. This happened to be a budget deal that was not my deal. I had decided I was going to vote against it. But it is easy when you are on the outside to be critical. I think the plain truth is that the goal of collecting the tax in a more efficient way is not a bad goal. I just think that whatever staff member was putting this together did not understand the implications of what was being done to nonhighway users of diesel. I think the plain truth is that the Congress dropped the ball. That happens.

I think the key is to go back and fix it. I think if we do not go back and fix it just because people do not want to admit a mistake, I think that at that point we have a real problem. Fortunately, the new law does not go into effect until April, so we have time to fix it. This could be one of those happy occasions where we fix something before the public knows it is broken.

Mr. DREIER. Well, I guess this is just another example underscoring what the President did in his State of the Union Message, the size of those two pieces of legislation which he had sitting next to him.

You mentioned April and April Fool's Day is your target date for repeal, and I wondered how realistic that is.

Senator GRAMM. Well, I have never believed that those who govern on the basis that most Americans are honored on that esteemed day were right. I don't think the American people are fooled on this issue. I think a lot of farm groups, the Farm Bureau and others, IPAA and the petroleum industry, and the fishing industry are aware of it. Obviously, they are really going to be aware of it when they start having to pay that tax. I mean we are going to be literally covered up with mail by the middle of April unless we do something.

I am hopeful that we can do something before that happens, and I think because all these groups have gotten organized, we have an opportunity to do that.

Mr. DREIER. Thank you very much.

Chairman HATCHER. Mr. Martinez.

Mr. MARTINEZ. Thank you, Mr. Chairman. Let me first say that I have always been impressed with your work and activity in the area of tax and that today you will probably be the only tax expert that we will have before us. So, I would like to ask you about providing a more efficient way to collect the tax.

It seems to me that sometimes what people do in reaction to a problem is an overreaction and creates more of a problem than there was initially. They really should have worked on correcting the problem that existed.

I was in business in the State of California for 23 years before I was fortunate enough to get elected to Congress. My business bought supplies and materials wholesale. When I sold my goods as retail products, I collected sales tax. I, in turn, was responsible for returning that sales tax to the State Board of Equalization.

The supplier from whom I bought my goods and supplies, wholesale supplies on which I did not pay tax, also occasionally sold goods and supplies retail. In fact, he sometimes sold both wholesale and retail to that same business. Items for that business' personal use would be retail and thus taxable because that person did not use them in comprising a product that he was going to sell.

The situation we are discussing today is similar. In this case, the dealer is selling wholesale to farmers and retail to others. But that wholesaler, like the wholesalers with whom I did business, knows his regular exempt purchasers, In addition, in California, we all had to get an identification number from the Board of Equalization. The Board of Equalization, a State agency, was responsible for making sure that we were entitled to the sales tax exemption, that we actually had a place of business and were doing business.

Therefore, it seems to me that there is already in place a system by which we could identify the persons who merit the fuel tax instead of saying, "We will collect the fuel tax from everybody, and we will pay back those that do not deserve to pay."

I have to agree with you. When I was in business, I never liked the Government using my money before I got a chance to use it.

Senator GRAMM. Well, if I were guessing, Mr. Martinez, I would guess that there was a target of a certain amount of revenue that they wanted the Joint Tax Committee to score. My guess is that some clever staff guy came up with an idea of simply changing the point of collection and said, "We can score that for a certain amount." And that nobody ever thought about the impact that was

going to have on exempt users. I was not involved in it, but if I were guessing, I would guess that is what happened.

I would never say that the collection system could not be improved, but I think going to the wholesale collection clearly has this problem that we are all here talking about. I do not think it was properly understood; otherwise, I do not believe Congress would have done this.

Mr. MARTINEZ. I agree with you. Thank you, Mr. Chairman.

Chairman HATCHER. Mr. Combest, do you have any questions from the Senator?

Mr. COMBEST. I have none. Thank you, Mr. Chairman.

Chairman HATCHER. Again, Phil, thank you for being here. We appreciate your testimony.

Senator GRAMM. Thank you, Mr. Chairman.

Chairman HATCHER. The next witness will be Representative Daub.

TESTIMONY OF HON. HAL DAUB, A REPRESENTATIVE IN CONGRESS FROM THE STATE OF NEBRASKA

Mr. DAUB. Mr. Chairman, thank you very much for allowing me the opportunity to testify in front of my old committee. It is good to be back. I want to commend you for your interest. The preparation, clearly, from the list of panels and witnesses that you have engaged in to fully air this, to be the first committee in the House to take a good look and build a record so that all of our colleagues can appreciate the difficulty that has been created and what needs to be done to correct it. I particularly want to give my encouragement to a member of this subcommittee, Mr. Combest, for the leadership he has shown in developing very definite language that can aid my committee, the Ways and Means Committee, in solving the problem that we face.

As a member of the Ways and Means Committee, I have been particularly outraged by the actions of the committee in passing this new provision which will effectively increase farmers' fuel costs by approximately 15 percent beginning on April 1 of this year.

I would like to inform you today that I have had a series of meetings with Internal Revenue Service Commissioner Gibbs over the past few days and have asked that he aid us by providing a temporary stay to the imposition of the tax until Congress has had the opportunity to address the issue. The Ways and Means Committee takes up tax legislation later this month.

I regret that, although the Commissioner was sympathetic to the plight of farmers and those in the construction industry and related businesses affected by these provisions or the omission of specific guidance to the Commissioner, he felt that he could not take the law into his own hands, so to speak, and he told me that Congress would have to address the problem legislatively.

Unfortunately, I do not expect my committee to begin markup of a tax bill until the end of this month when we take up technical corrections, again. The fact is that barring unusual remedy, this law will not be repealed until after the effective date, April 1, passes.

It is my hope and my recommendation that this committee request the chairman of the Ways and Means Committee to take immediate action to repeal this unfair tax before the administrative problems of this provision begin.

I would also note that the plight of the farmer, in particular, is an unusually difficult one. Consider this: Farmers do not file estimated taxes. Neither do they have withholding from wages as do most Americans. Instead, Congress imposed an earlier filing date for farmers to file their tax returns. The date, just past, is March 1. I hope you are thinking through with me, now, what kind of problems there are starting to be created by this.

In short, farmers have an exaggerated cash-flow problem because they must wait the entire year in most every case before they can receive the money due them which they never did owe. Taxpayers who make estimated tax payments can reduce the amount of their quarterly filings. Taxpayers who have withholding can increase the number of exemptions claimed on their W–4 form to take into account the amount of increased taxes paid through the diesel fuel tax. Farmers have no such opportunity.

My point from all this is that farmers are an extreme case crying out for extreme relief. Soon, they will begin paying a new tax which will add to their cash-flow problems, their interest costs, and their administrative filings with the Government. This is a revenue issue, but it is not a compliance problem. Farmers do not use diesel fuel for road use, and, so, they are not being penalized for noncompliance.

This is purely a cash-flow issue, and the Government will be funding itself on the float of the American farmer's money. The acceleration of the payment of this tax followed by its refund because of the timing of the Government's fiscal year results in about a $100- to $150-million gain to the Government during fiscal 1988. In later years, this provision will actually lose revenue, I am told.

This is ridiculous tax policy. My bill, H.R. 3844, properly addresses the issue. It is the earliest numbered bill, the earliest filing. We have about 65 cosponsors now. We attempted to make it the most comprehensive in terms of drafting language. We have carefully thought out the implications and done the estimates to try to figure out the right ways for our committee to be able to quickly deal with the problem. It addresses the problems that Mr. Combest and Mr. Schuette are very concerned about, and that is, generally, the gasoline tax, not just the diesel tax, for offroad onfarm use.

Let me also add that my bill addresses problems in the tax on gasoline tax that you may know about that is also now to be imposed on blended fuels. The ethanol-alcohol or gasohol tax has now been equalized and so, the blender at point of distribution must offer to collect the tax, must collect the tax, and then can file for a refund 21 days later.

The Commissioner of the Internal Revenue Service did, yesterday, grant us a 3-month extension and has agreed not to publish the anticipated set of regulations on the tax to be imposed on ethanol or blended fuels for 3 months, appreciating the problems that would occur to that industry, certainly of enormous and catastrophic impact if that proposed set of regulations had been published to take effect to collect the tax on April 1, just as the diesel

tax we are talking about. So, at least a little good news in that regard.

Finally, I will add that my bill also includes a very important provision for hundreds of small businesses that are suffering from the negative float of this tax. These businesses are petroleum marketers, and I believe that many of them will be driven out of business without this provision being passed. It has been coined as the "Pickle Amendment," after my colleague on the Ways and Means Committee who first introduced it. I look forward to the testimony of the Petroleum Marketers Association later in this hearing regarding this important provision for small business.

Let me say that there was a good deal of thought by someone in that clandestine operation, in response to Mr. Dreier's question. That is to say that neither the House nor the Senate in the committees of jurisdiction nor on the floor in debate really addressed the issue.

So, there is a real question as well, I say to my colleagues, about process, that the light of day never did get to shine in on this provision except that in the technical marking up of the conference, somebody decided that airplanes and trains do not use the roads, so, they ought to be exempt, that certain Government municipal vehicles ought to be exempt, and certain industrial uses also ought to be exempt. Actually, there are four exemptions written in and were written in by staff or by someone in that conference. No one quite knows, really, why clearly the other concerns that are being brought to your committee today were not addressed.

So, I really want to conclude by saying that you are doing a great service to Congress, the country, and many businesses and industry.

Chairman HATCHER. Thank you for your testimony.

Mr. Dreier, do you have any questions?

Mr. DREIER. Yes; thank you very much, Mr. Chairman.

Thanks for your testimony, Hal. Welcome back to the Small Business Committee. I just wanted to follow up on what you just mentioned and what we went through with Phil, and that is, I understand that last June the Joint Tax Committee put a booklet out in which they specifically outlined this provision and the recommendation.

I do not mean to be pointing the finger at anybody. You are the only one in the room from the Ways and Means Committee.

Mr. DAUB. I understand.

Mr. DREIER. Was this part of any kind of package thing? You say it did not come up in either committee. It did not come up on the floor. Did the administration have a position on this particular provision?

Mr. DAUB. It was actually not a part of the bill that came out of the House, the committee or the House. There were compliance areas that were raised. I can see how they could argue in conference that there was scope, with all due respect, because—again, as I think Senator Gramm said, there is an objective here. There is abuse. There is use of the purchase at the point of distribution of fuel that actually does get used in vehicles that operate on the roads and create the crumbling and the chuck holes, and there is a trust fund solvency issue that we must always be mindful of. So, I

believe that there was an objective there that was worth pursuing. But this is overkill.

The actual House committee did not take up the matter. I raised it at final passage in committee on reconciliation, voting no, then. Concerned not about the omission but the lack of specificity. I was worried that deep down in the bowels of the Treasury, there would be folks down there that would see their opportunity, much as the 1099 issue you raised or the automobile vehicle mileage recordkeeping requirement that was the result of regulations published from a law that was well-intended.

You remember. That law was very clear. We were looking for Cadillacs and Mercedes Benz that were in the country club parking lot at 10:00 in the morning for brunch on Sunday, but they never showed up in the company parking lot on Monday morning at 10 a.m., giving the owner the benefit of the doubt, but they were being written off as an expense of doing business. We tried to get at that. From it came those regulations that wanted mileage books kept under our pillows for cherry pickers, backhoes, combines, and emergency vehicles. It was really just simply not what was intended. That is what has happened here.

There was some intent to pursue compliance and, indeed, lack of consideration in the committees in process. Beyond that, again, the accident of letting some unappointed, unelected official work up a grab at revenue. I think you and I have seen that happen all too often around here. I think that is really enough of the answer at this point. We know the problem and now what we have got to do is get on about it and fix it.

Mr. DREIER. I just think it is important for us to realize that a year ago this was made public, that it was under consideration.

Mr. DAUB. Yes; and that we specifically were careful in our own House deliberations not to include it. We were aware of some who were interested in getting that revenue. We thought we had succeeded in preventing that particular provision or the regulations that may be published pursuant to it from getting into the law. Now we find out, again, in the eleventh hour, as I described it, the Trojan Horse, with real deep legs, and a soft underbelly, and thousands and thousands of line items were tucked into that bill with 1 hour of debate and one vote, closed rule. The chance for the light of day to shine in certainly did not exist.

Mr. DREIER. Thank you very much, Hal. Thank you, Mr. Chairman.

Chairman HATCHER. Mr. Combest.

Mr. COMBEST. No questions, Mr. Chairman.

Chairman HATCHER. Well, thanks again.

Mr. DAUB. You are very welcome, Mr. Chairman.

Chairman HATCHER. Thank you. Mr. Jontz.

TESTIMONY OF HON. JIM JONTZ, A REPRESENTATIVE IN CONGRESS FROM THE STATE OF INDIANA

Mr. JONTZ. Thank you, Mr. Chairman. I want to express my appreciation to you and the other members of this subcommittee for allowing me the opportunity to testify this morning. You are to be commended for recognizing the problem that has been created for

America's farmers and small businesses by the provision in the Budget Reconciliation Act that can now be found in section 4093 of the Internal Revenue Code. I hope that the attention that is created by this hearing will result in delay of the April 1 implementation date and will lay the groundwork for a legislative solution to this problem.

I also want to recognize the efforts of my colleague, Mr. Combest. The legislation which he has introduced to deal with this problem has received considerable support from his colleagues, as we have heard this morning. Last week, Mr. Combest, Mr. Daub, and Mrs. Smith joined me in sending a letter to Chairman Rostenkowski about the problems created by section 4903.

On the first day of this session of the Congress, I introduced H.R. 3850. Its purpose was very straightforward: To prevent farmers from being required to pay diesel fuel excise taxes on fuel purchased for offroad use. Support given to this bill has been gratifying. Just about 70 of my colleagues have joined me in cosponsoring H.R. 3850, and the bill has been endorsed by all of the major agricultural groups in our country.

What has brought organizations as diverse as the American Agricultural Movement and the American Farm Bureau together is the recognition of the great hardship which section 4903 will cause for our Nation's farmers. It is estimated that about 1.2 million farmers are going to be unnecessarily charged around $420 million a year in excise taxes, money which does not and will never belong to the Federal Government.

We are told that the reason behind this new tax collection system is to reduce tax fraud and to make it easier for the IRS to collect excise taxes. Yet, the individual who is cheating on his taxes now can still cheat by filing a false report under the new provision.

We are all against tax fraud. Surely, the IRS could devise a system to effectively reduce abuse without penalizing all farmers, the vast majority of whom are honest.

I do not doubt either that reducing the number of collection points for diesel excise taxes will make it easier for the IRS to collect these taxes. But is it fair to ask American farmers to pay $420 million in taxes every year simply for the convenience of the IRS? As has been pointed out before, this amounts to an interest-free loan from the farmers to the IRS. I have been looking around the Fifth Congressional District of Indiana, and I have not found any of our local lending institutions that are making interest-free loans at this time.

In a letter that I sent last week to Commissioner Gibbs, I pointed out that it is ironic that this change is being made at the same time the IRS is trying to convince individual taxpayers to fine tune their withholding to match the actual amount of tax owed. As you know, this is one of the major reasons for the adoption of the new W-4 forms. However, with this new excise tax requirement, farmers are going to be paying taxes that they do not owe. A vast new tax collection refund system will have to be created to administer this.

It is notable that last week, Commissioner Gibbs told a subcommittee of the Ways and Means Committee that changes to the Tax Code are causing even bigger headaches for taxpayers. When tax-

payers can get through on the telephone to the IRS, sometimes the answers they get are wrong.

Now, the same agency is going to require farmers to keep new records, file new forms, and then hope they get their money back, without any interest.

Very few Members of the Congress knew about this provision in the Budget Reconciliation Act. We do know about it now, and, if we act quickly, we can spare American farmers and small businesses the problems that will be created by section 4903. I hope that this hearing will lead to a quick resolution of this problem through the passage of corrective legislation.

Again, Mr. Chairman, I thank you and the members of the subcommittee for the opportunity to testify today.

[Mr. Jontz' prepared statement may be found in the appendix.]

Chairman HATCHER. Well, thank you for being here and for your testimony.

Mr. Combest, do you have any questions?

Mr. COMBEST. No, sir; thank you.

Chairman HATCHER. Thanks again, Jim. Thanks for being here.

Ms. Schneider, I would like to welcome you to the subcommittee and look forward to hearing your testimony.

TESTIMONY OF HON. CLAUDINE SCHNEIDER, A REPRESENTATIVE IN CONGRESS FROM THE STATE OF RHODE ISLAND

Ms. SCHNEIDER. Thank you, kindly. I appreciate the opportunity to testify, and I congratulate you for holding hearings on this matter.

I, like my colleagues before me, want to share their enthusiasm for the support of our colleague, Mr. Combest.

Rather than elaborate on points that have already been made, let me just share with you some of the grave concerns that I have regarding the impact on a particular segment of our society, and that is the fishing industry.

The aspect of the regulation's impact that I would like to focus on has to do with the commercial fishing industry which brings at least $14 billion into the U.S. economy each year. Approximately 130,000 fishing vessels throughout the United States would be impacted by this new regulation.

I think it is important to note that at this time we are becoming much more sensitive to what it takes for the United States to be more competitive with our foreign allies. There is no question that the commercial fishing industry is the only sector of the U.S. economy with a trade surplus with Japan—a $1.1 billion surplus in 1987, and the industry is comprised almost exclusively of small businessmen. I think that the new regulation that is to take effect on April 1 requiring fishing vessels and other nonhighway users to pay a 15.1-cent-per-gallon excise tax on diesel fuel on a quarterly basis is entirely inappropriate. This money will be deposited in the Highway Trust Fund which will benefit from the accruing interest, and the fishermen will have to wait and apply for a refund.

Just to give you a little bit of insight as to what that means to your small businessman or the average fisherman, many fishermen are already operating on a very narrow profit margin, and fuel

comprises 27 percent of their operating costs. So, it will obviously have a major impact on their cash-flow that will also mean the loss of their accruing interest. Needless to say, fishermen do not exactly have the time to do extra paperwork.

I think we also need to point out that much of the fuel that is purchased is sold on credit. So, we are talking about a second layer of paperwork that would then be generated. There is also a problem with the 1988 budgets that most fishermen have already accounted for without this new tax.

The fishing industry, as I said, provides the United States productivity margin with an added advantage because we do have a trade surplus in this area. There is no question that unless we move ahead on the Combest proposal, we are going to jeopardize yet another segment of the small business community, a segment that already has a lot of problems.

In the last 2 weeks, alone, the committee on which I serve, the Merchant Marine and Fisheries Committee has dealt with the escalating insurance costs to the fishermen, not to mention the challenge of dealing with some of the contaminated sewage sludge that is being dumped and also cutting down on the productivity margins of the fishing industry.

So, I urge all of you to move this proposal ahead, and, certainly, you can be assured that the commercial fishing industry is 100 percent behind the passage of it.

[Ms. Schneider's prepared statement may be found in the appendix.]

Chairman HATCHER. Thank you very much for being here and for your testimony.

Mr. Dreier.

Mr. DREIER. Thank you very much, Mr. Chairman.

I would simply like to congratulate you, Claudine. We see now that not just farmers and small business people in other areas of the country, but, specifically, in New England, we are seeing a very detrimental impact of this tax. I would like to thank you for bringing to our attention something which otherwise probably would not have come before us. Thank you.

Ms. SCHNEIDER. Thank you, kindly.

Chairman HATCHER. Mr. Combest.

Mr. COMBEST. No questions.

Chairman HATCHER. Again, thank you for being here.

Ms. SCHNEIDER. I appreciate the opportunity, thank you.

Chairman HATCHER. I think before we call the next panel, we will just stand at ease here for a minute and see if there is a vote journal.

[Whereupon, a brief recess was taken.]

Chairman HATCHER. We will reconvene at this time, if we have the next panel here. Mr. S.M. True, president of the Texas Farm Bureau, representing today the views of the American Farm Bureau Federation. Mr. Harry Spannaus. Did I say that right?

Mr. SPANNAUS. Yes, sir; thank you.

Chairman HATCHER. Executive vice president, Permian Basin Petroleum Association, and Mr. Gene Hutter, north central regional vice president, Petroleum Marketers Association of America.

Unless you gentlemen have some other preference, we will hear from you in the order in which your name was called. Could you all stay here until you three are finished. If so, we will hear from you without questions and save the questions until the end of the three. Mr. True.

TESTIMONY OF S.M. TRUE, JR., PRESIDENT, TEXAS FARM BUREAU, ON BEHALF OF AMERICAN FARM BUREAU FEDERATION

Mr. TRUE. Thank you, Mr. Chairman, and members of the subcommittee. My name is S.M. True. I am a farmer and a rancher from Plainview, TX. I operate a medium-sized, cotton, wheat, feed grains, and cattle operation. I am president of the Texas Farm Bureau, and, today, I am representing the American Farm Bureau Federation, the Nation's largest organization of farmers and ranchers.

I am also a constituent of Congressman Larry Combest, and I must say that I am proud to be one. I appreciate his leadership on this important issue. I also appreciate Chairman de la Garza and Senator Gramm in their leadership. We thank you, Mr. Chairman, for holding this hearing for us.

I am here today to share with you the Farm Bureau's concern over an obscure provision of the Omnibus Budget Reconciliation Act of 1987 which will have a profound impact on millions of farmers and ranchers. This provision changes the collection point for diesel fuel tax from the retail level to the wholesale level. Beginning April 1 of this year, farmers will be forced to pay a 15-cent-per-gallon excise tax on diesel fuel and then file for a refund or a credit. Farmers now have an excise tax exemption for offhighway uses of diesel fuel.

Today, we are asking your favorable consideration of legislation that will permit farmers and ranchers to continue to buy fuel tax-free if it is used for offhighway purposes. If this provision is not changed, farmers and ranchers will be burdened with an additional operating expense which will total hundreds of millions of dollars in diesel fuel excise taxes. Although farmers will be able to apply for refunds of these taxes, cash-flow problems and higher interest costs to agricultural producers will undoubtedly result.

Costs to agriculture would be substantial. According to the 1982 Census of Agriculture, annual farm diesel fuel use is approximately 3 billion gallons. At 15 cents per gallon, agricultural producers would be forced to pay approximately $400 million in diesel taxes, and in my home State of Texas, the impact to agriculture would be about $30 million. On my farm, which is a fairly typical operation, my offroad diesel fuel consumption per year is approximately 8,346 gallons. This means that I will be forced to pay about $1,251 in taxes to the Federal Highway Trust Fund for fuel used off the highway on my farm in the production of crops and livestock. Included in my statement for the record are State farm diesel fuel use figures from the 1982 Census of Agriculture. These statistics dramatize the impact of this new tax on farmers nationwide.

This is a tax that farmers do not owe and should not have to pay. It means that I must borrow additional operating capital and that I

will have to pay higher interest costs. It means additional regulation and paperwork to obtain a refund.

Timing could not be worse. This new expense and regulatory burden will be imposed when farmers must cut expenses and increase efficiency in order to survive.

Although many of the details of the refund system to be imposed are not yet clear, there may be some major inequities. The Internal Revenue Service has informed us that farmers may file for a quarterly refund if the refund for the quarter is $1,000 or more.

This would require diesel fuel use of at least 6,667 gallons per quarter or about 26,667 gallons per year, and only the very large farmers use this much diesel fuel. In checking with USDA's Office of Energy, we have estimated that less than 20,000 farmers would qualify to file for a quarterly refund. Most would have to wait until the end of the year and then file for a tax credit on IRS Form 1040.

Last, I would like to bring to your attention a problem which underscores the need for quick legislative action to restore the previous tax-free purchase method of diesel fuel for offhighway use. An excise tax for offroad diesel fuel could increase fuel costs and disrupt the distribution system. This could occur when farmers and other offroad users top off their storage tanks just before April 1 to avoid paying the extra 15 cents per gallon. This could create sudden artificial demand for billions of gallons of diesel fuel which could not be supplied by the current refining and distribution system.

This problem could be especially serious since it would take place in the early spring, the peak fuel use period for spring planting.

Additional strong demand will also exist during the same period for home heating oil, which is essentially the same product as diesel fuel. Higher diesel fuel prices and regional shortages could result.

Mr. Chairman and members of the subcommittee, the new requirement for collection of farm diesel fuel taxes is unfair, and it is of questionable benefit to the Federal Government. It will create a new financial and regulatory burden on farmers and ranchers. It will increase production costs and may cause serious disruptions in fuel supplies which are essential in the production of agricultural commodities.

These concerns are shared by 15 other major organizations which have cosigned a letter to all Members of the House and Senate expressing the need for immediate action.

Several bills which would accomplish this objective have been introduced and, although the language of these bills is different to some extent, it is our understanding that each would restore the tax-free purchase of diesel fuel used off the road in the production of agricultural commodities. I am certainly appreciative of Congressman Combest for his prompt action in introducing H.R. 3865 to deal with this problem.

April 1, Mr. Chairman, the implementation date is fast approaching, and we appreciate you holding this hearing to call attention to this problem. Thank you, sir.

[Mr. True's prepared statement may be found in the appendix.]

Chairman HATCHER. Thank you for your testimony, and thank you for being here today.

Mr. Spannaus.

TESTIMONY OF HARRY A. SPANNAUS, EXECUTIVE VICE PRESIDENT, PERMIAN BASIN PETROLEUM ASSOCIATION

Mr. SPANNAUS. Chairman Hatcher and subcommittee members, thank you for this opportunity to appear before you today. I am Harry Spannaus. I am employed by the Permian Basin Petroleum Association with headquarters in Midland, TX.

Our association has over 1,300 members composed of both major oil companies and small independent oil and gas producers and related service and supply industry members such as drilling contractors.

The Permian Basin is the largest single crude oil and natural gas producing region in the lower 48 States both in size and production. It encompasses 54 counties in West Texas and 4 counties in New Mexico, covering over 100,000 square miles. It produces approximately 23 percent of all domestic crude and 15 percent of all natural gas.

I am also testifying on behalf of the Texas Independent Producers and Royalty Owners Association, the Kansas Independent Oil and Gas Association, the North Texas Oil and Gas Association, the Independent Petroleum Association of New Mexico, the West Central Texas Oil and Gas Association, East Texas Producers and Royalty Owners Association, the Panhandle Producers and Royalty Owners Association, and the Coastal Oil and Gas Association whose combined membership exceeds 10,000 members.

We commend the subcommittee for conducting this hearing. We believe it is important in this time of domestic petroleum industry depression to take whatever measures that are reasonable and necessary to provide a fair and just taxation treatment to an industry that is already on its knees and fighting for recovery.

The new law to collect up-front taxes for previously exempt off-road diesel fuel is another among many rules and proposals which will have a negative impact on our industry, especially the drilling contractors and the various wells servicing companies who consume large quantities of diesel fuel for drilling and downhole servicing operations.

Before I get into specific effects that the new tax ruling will have on much of the industry, I want to provide you a brief summary on the health of the domestic petroleum industry. More especially that of the Permian Basin of which its primary industrial base is that of oil and gas, but also the domestic industry throughout major producing States in the Nation, as we all face similar difficulties.

The contract drilling and well servicing industry is in bad shape. The Western Co., one of our largest well servicing companies, just recently filed for chapter 11 bankruptcy. Several of our drilling contracts such as MGF and Loffland Brothers, have been under chapter 11 procedures and constraints for many months. Today, they are still struggling for their survival. Within the Permian Basin, nearly 40 percent of our firms engaged in drilling and well services just a few years ago, are now out of business. Their plight is shown most dramatically by the Basin's daily operating rig count

which went from a high of 529 in January 1982 to a low of 74 in September 1986. Today, it is now fairly constant at 145 operational rigs.

In Midland, TX, our second largest employer of employees continues to be the FDIC which quarterly holds the Nation's largest garage sale and where auction sales revenue comes from goods and equipment obtained from foreclosures and failures of petroleum industry businesses.

Bank failures have hit an all-time high in Texas and most producing States, as have business failures. In short, we need sound legislation to enhance our industry, not additional tax burdens which will increase outgoing cash-flow without revenue generation in return and added operational costs for governmental compliance paperwork.

We believe the subcommittee would like some 1987 statistics that it could work with. Some realtime figure data which is used in forecasting the adverse effects of the new pretax requirements on off-road diesel fuel purchases.

We have obtained our data from two small independent drilling contractors, namely, Gene Sledge Drilling and Peterson Drilling of Midland, and two of our largest service companies, the Western Co., which recently filed chapter 11 for reorganization and Halliburton Services, who for the first time in several years, reflected a 1987 profit in sales and services nationwide.

I request the subcommittee to refer to exhibit A, if you have that near you.

As per exhibit A, both drilling companies described are relatively small companies, having only four to five rigs in inventory with a utilization rate of approximately 75 to 80 percent of total capacity.

As you will note, each drilling company consumed in excess of 650,000 thousand gallons of diesel fuel with an average rig daily consumption rate of over 500 gallons. Considering actual 1987 data, if an excise tax of 15.1 cents per gallon was levied on Gene Sledge Drilling for 1987, the company's total additional cash-flow outlay would have been $107,000 or $21,400 per operational rig.

If you assume that each Gene Sledge rig was operating fulltime, a situation which we really hope to recapture, the company's additional cash outlay due to the imposition of the excise tax on diesel fuel would be approximately $142,000 a year.

In the case of our service companies, exhibit A depicts figures on a national basis. It is understandable by these exhibits that the additional cash-flow burden could be devastating, especially to those small independents or companies faced with chapter 11 proceedings or who have operated near or in the red for 1987.

From all known estimates from economists and other experts such as the American Petroleum Institute, Petroleum Information, World Oil, and the Oil and Gas Journal magazines, the drilling outlook and well-servicing projections for 1988 will be much like that of 1987, and the industry will continue to struggle for profits.

The addition of the excise tax on exempt fuels and the corresponding costs for compliance may only hasten the inevitable—that of further business crisis or total failure.

The Western Co. is currently operating under bankruptcy reorganization procedures and not only has not programmed or budgeted

for additional annual cash-flow of over $340,000 to meet excise tax requirements, but it can ill afford the added expense burden when their reorganizational program is overseen by the courts and is one of austere cuts and reductions in support of its recovery efforts.

Halliburton Services, a division of the huge Halliburton companies complex is much more capable of absorbing the increased cash-flow requirement within its organizational structure. However, it was only until recently that it showed an annual profit and an additional liability of $1 million and the burden of added administrative costs would be a further detriment to its continued recovery efforts.

The small independent drilling companies and others who are in financial difficulties are not sure how they are to meet this added taxing obligation.

Regardless of their ability to recover such taxes by filing for refunds following the year's end, the money has not been budgeted nor is there sufficient reserve funds available to cover the added liability. To borrow the money from a banking institution, which would be next to impossible in today's times, would be adding additional cash-flow liability and interest and would only deepen the wound about to be inflicted.

The remaining way is to charge back to the customer to recover the additional costs, a procedure totally counterproductive as it would destroy the small independent's ability to compete in a highly competitive marketplace.

While offshore drilling operations are far distant from the Permian Basin, the same problem is shared. According to the International Association of Drilling Contractors, a drilling contractor having a fleet of 20 offshore drilling rigs would use approximately 500,000 gallons of diesel per month with additional tax costs of over $900,000 per year.

In summary, we believe that a tax levied on the tax exempt commodities such as diesel fuel, for the identified purpose of stopping the widespread evasion of diesel fuel tax payments to the Federal Government is unfair. It is unjust, and it is a depressant to business enhancement.

It is an action which places an undue burden on the majority to aid the IRS in the internal difficulties of their detection and collection process.

While we cannot say that such evasions do not occur in the oil patch, it is highly unlikely that diesel fuel used to operate well-site equipment is being used for onroad purposes, just as it is also unlikely that diesel fuel or heating oil used for home heating is also being used for onroad motorized vehicles. There are numerous safeguards to prevent such evasions, fully qualifying petroleum industry motorized offroad equipment in a category which most likely will not utilize offroad diesel fuel for onroad purposes. I will be most happy to further discuss these safeguards following this prepared testimony.

And, last, we believe that a permanent fix to the new tax would be an outright repeal of the collection point for Federal excise taxes on diesel fuel as required by the Budget Reconciliation Act of 1987.

Knowing of the difficulties of such a repeal, the next best alternative would be to provide an amendment to the bill such as H.R. 3865 proposes, which would permit tax free sales of diesel fuel for offroad uses or influence the Department of the Treasury to exempt the petroleum industry and others from such taxes as currently exists and as what is thought to be a granted authority by the Congress.

Thank you for your invitation to appear before you. I will be most happy to respond to any questions you may have.

[Mr. Spannaus' prepared statement, with attachment, may be found in the appendix.]

Chairman HATCHER. Thank you, and we appreciate your testimony. Mr. Hutter.

TESTIMONY OF GENE HUTTER, NORTH-CENTRAL REGION VICE PRESIDENT, PETROLEUM MARKETERS ASSOCIATION OF AMERICA

Mr. HUTTER. Good morning, Chairman Hatcher, and other members of the subcommittee. I have a written statement, and I just cannot stay with it. You stop me when you want to, sir, and I will stop. But there, look at the reaction. That is a copy of the Farm Bureau and the House bills that have been introduced and the Senate bills that have been introduced. I share your disappointment that the IRS chose not to appear here.

I wonder if there is a member of the IRS in this room because I am going to tell you a story now that is a fact. In late January, we hold the winter board or directors meeting for the Petroleum Marketers Association of America. I am sorry, and I will get to better identifying myself, but I want to tell you these things before I forget them. I cannot ever forget them, really, but I can forget to tell you.

We were privileged to have two members of the IRS appear before roughly 500 of us who attended the winter board meeting held here in Washington to answer our questions because as of January 5, IRS had not issued any final regulations as to how they were going to handle this excise tax payment on gasoline. I want to be sure before I leave here that you truly understand what has happened in this whole system.

So, we thought, late January, maybe we could talk about diesel then and get some knowledge. All right? We got very little knowledge. But our Senator, Alan Dixon, and he did not attend, but two of his aides did, Chuck Pizer and Mark Urean. So, after this session, we had lunch, and I wanted to know before any words were spoken what these two men who had to go back and report to the Senator thought of how the two IRS representatives conducted themselves and of what benefit they were to 500 of us gathered looking for information as to what is going to happen to us. I said, "Put it to us in as few words as possible."

And Chuck said, "I can do it in one." And the word was, quote: "Antagonistic." End quote.

Now, what a system. What a system we have. That is what 500 of us were privileged to. So, I do hope someone is here from the IRS so they can take that back to whomever should have it.

It has been said by some of the members who testified that they were fixing it, and we do no know what we are fixing. Back home we say, "If it ain't broke, don't fix it."

We had a system of remitting Federal excise tax on motor fuel that worked fine. It worked just fine. Because there were some people in Florida and the east coast, New York, particularly, who evaded those taxes, this became a vehicle to change the method of collection.

The IRS contended that they are unable to audit 11,000 marketers, people like myself. So, if the tax could be collected by a lesser number, and that number is about 400 of the suppliers or refiners, if you please, then that is the way it ought to be done. Then it would be simple. It would all be collected.

That is a Utopian idea because crooks are crooks, and they are going to figure out ways to evade taxes forever more.

My question was: How can the IRS send Wanda and me, that is Mrs. Hutter, a bill that we owe them $385 from 1986 if they cannot audit 11,000 businesses? How many taxpayers in the United States? 100 million? 150 million? I do not know. I really do not. But if they can trace everybody—and they do—and maybe some of the others in this room have been called in and said, "Hey, your tax return is wrong."

All right, with that background, I will go on to this statement, and I may skip part of it because if I come to a point that is just repetition, it will be deleted.

I am Gene Hutter. I am executive vice president and general manager of the Wally Hutter Oil Co., petroleum marketer in Quincy, IL. I will tell you where Quincy is. It is 100 miles west of Springfield, IL, 200 miles east of Kansas City, 300 miles south and west of Chicago, and 125 miles north of St. Louis. The nearest express 4-lane highway is 70 miles away. We market in Missouri, Illinois, and Iowa, and we do represent agriculture.

Of particular importance to the subject of this hearing is that we have over 1,000 farm accounts. We have two subjobbers we supply and through those, in our business, that represents about half of our total business.

We also have 300 heating oil accounts, and they are practically all rural. You are going to say, "Why rural?" Because the utility company came in, put in a gas line and 25 years ago almost everyone switched to natural gas.

I am here this morning in my capacity as the north-central regional vice president of the Petroleum Marketers Association of America, approximately 11,000 small independent businessmen. The last 3 weeks, I visited the meetings in Iowa, Missouri, and just yesterday, Ohio, and believe me, this taxation thing on diesel and motor fuel has an extremely high profile.

Collectively, we marketers account for approximately 50 percent of the gasoline, 60 percent of the diesel fuel, and 75 percent of the home heating oil sold in the United States of America. We commend this subcommittee for its active interest in the Federal Diesel Fuel tax issue. I also commend you for your knowledge.

I became depressed in October 1986 when I first met a committee and found out what was going to happen to us, and God bless Jake Pickle, he delayed it a year by getting an amendment which on the

gasoline tax revision carried it over to January 1, 1988, as opposed to January 1, 1987. I cannot speak highly enough about Congressman Pickle and his efforts on our behalf.

The PMAA has been working on motor fuel excise tax collection issues for several years. Our efforts have been directed at both the revisions in the collection process for the 9.1-cents-per-gallon Federal excise tax of gasoline as well as the more recent provisions in the collection procedure for 15.1-cents-per-gallon excise tax on diesel fuel. The written statement details concerns in both areas, but in the interest of time, I am going to focus my remarks on the change in diesel fuel tax collection procedure.

Section 10502 of the Omnibus Budget Reconciliation Act of 1987 substantially altered the way diesel fuel excise taxes are collected and remitted to the Federal Government. As a marketer, we did not pay them. We do not pay them now. April 1, we will.

Under this provision, the diesel fuel excise tax will be collected by the producer. The term, "producer," is defined to include refiners, terminal operators, et cetera, et cetera, who will post a bond required by the Internal Revenue Service.

In addition, this provision requires that effective April 1, all current tax exempt purchasers, farmers, drilling contractors—you know them all. You have heard about it already. I even talked—what was the Congresswoman's name? Schneider? Just this morning before I left our office down the street, I called Bill Gresham, Mississippi, and amazingly he has the same problem in Mississippi, and she is from Connecticut or Rhode Island, as I recall—fisheries. The fishing industry down there, and it did not occur to me, but Bill has that same problem down there, and he is just another marketer like the rest of us.

All retailers who currently have the right to pay the tax to the IRS must also pay it to the refiner or wholesale distributor. Residential home heating oil is exempt from the tax. Certainly, it ought to be, but I am surprised it is. If the IRS could figure out a way to drag it in, they would.

The Department of the Treasury has the discretion to exempt certain other users from payment of the tax, including State and local governments. All of the problems associated with this new collection procedure are not yet known. Despite the fact that this change is scheduled by law to take effect April 1, IRS has not, as of today, issued any proposed regulations or guidelines on how the procedure will work. Today is what? The 2d or 3d of March. January 5, we did not know on gas.

For example, what will—you do not want to hear that. It takes your time.

Prior to enactment, PMAA recommended that the effective date be no earlier than July 1, 1988, and preferably, 90 days after IRS was able to issue the final regulations to implement this proposal. As I understand, from listening this morning, that can only be done by a congressional rule. I am not optimistic that the law is going to be changed prior to April 1, so, we are encouraged that that be done and that the tax on diesel fuel remain the same for at least 90 days beyond April 1 until Congress can put the intelligence I have seen displayed here this morning to work, hopefully.

I am probably driving my colleague in the back there bats by skipping over this. I just do not want to repeat what has been previously said.

While we have no choice but to await direction from the IRS on certain issues, there are some obvious problems that will require statutory correction. The most obvious of these is the requirement that farmers, mariners, drilling contractors, et cetera, et cetera, pay the tax directly to the wholesale distributor.

This creates two tremendous problems. By the way, IRS, at the district office, is not even aware really how this is going to be handled. They do not know. They cannot help us out at the district office.

American farmers will be paying $420 million, somewhere between $420 and $450 million. Let me ask you, gentlemen, a question. I am supposed to be testifying, but I heard it said earlier in testimony that farmers are going to pay tax they do not owe, one of the earlier Congressmen. Are we not, as marketers, paying tax we do not owe? Do we owe this tax?

When I go to the terminal, the pipeline terminal with our transport and pick up 8,000 gallons of gasoline, and 10 days later Shell Oil Co. drafts my account for the gas and the Federal tax, I have not sold it. I still own it. Have I not advanced money to the Federal Government? Am I not in the same condition as the members of the American Farm Bureau Association, the farmers in America who are paying this in advance?

Another thing: Those of us in this business, and you will hear from another one from Georgia, carry some of our accounts crop to crop. The gentleman on the left, who is no longer here, my left, your right, said he did not know much about farming. He knew a lot about farming. He had a good understanding of it. But farmers do not get money every day of the week, or every week of the month, or every month of the year. If they are farming wheat, they harvest the wheat in the late summer, and we get some of the money for our fuel then. If they are on pigs and pigs have been great—during the last several months, in excess of a year, correct me if I am wrong, over $50, the economy has turned up a little bit. But you do not raise a hog for market in 6 weeks' time. They have got it down under 6 months, but nonetheless, they have to wait until then to do it.

I would make another point. Our farm economy is reported to be up. Farm economy in the United States of America, 4 to 6 percent in 1987 over 1986, brought about by demand for wheat, and better prices for livestock. Let us not reverse. This is the first the farmer has seen daylight in several years. Let us not reverse it by making him pay in advance. This is contrary to our way of life, our Government, everything about our country; but this is what we are proposing to do. In my little community, if the farmer does not do well, the small businessman does not do well. So, we all suffer.

Now, I am going to read what you are waiting to hear. Thank you, Mr. Chairman and members of the subcommittee. I will be most happy to respond to any questions you might have. Believe me, I am privileged to be here. I like being up in front because there is water to drink, but I will go away with an empty heart, if I have any feeling that you, Mr. Combest, you, Mr. Hatcher, any of

you do not understand fully what has happened in the last 14 months with this motor fuel tax collection.

[Mr. Hutter's prepared statement, with attachment, may be found in the appendix.]

Chairman HATCHER. I only have one question, Mr. Hutter. Did you send them the $385?

[Laughter.]

Mr. HUTTER. No, no; I will tell you what I did.

Chairman HATCHER. That is all right.

Mr. HUTTER. No; I am going to tell you. I did not owe it. I got back money.

Chairman HATCHER. I can tell you have given this a lot of thought, and it means a lot to you and to people in your area and, obviously, throughout the country, especially in rural America and where they fish. I learned more about the fishing impact today, too, than I had known. Your testimony is valuable, and we appreciate it, each of you.

Mr. Combest, do you have any questions of any of the panel members?

Mr. COMBEST. Yes, Mr. Chairman; thank you. I appreciate all three gentlemen coming to testify. You are bringing something to this I think is important. It gives me some hope that we can do something. You have energy from the production standpoint represented. You have energy from the marketing standpoint represented. You have agriculture represented. We had, earlier, as you both have indicated, fishing. We are going to have some others from the contracting industry. The change affects a lot of people.

I think what brought about this was the inability or lack of ability to collect some tax that everyone agreed was due. Many of the witnesses earlier today, and you, and others who will be testifying, are making suggestions regarding the way to handle collection.

It is not as if you do not want to help IRS in doing their job or enforcing compliance. It is just that we think that it would be a lot easier to comply in other ways. That is one of the reasons that I, as the chairman expressed earlier, am personally very disappointed that the Internal Revenue did not come so that we could talk about avenues with them that might be workable. To help ease some of their problem and help them collect the tax that is due without imposing the burden created by the new law.

Mr. True, in our private conversation earlier, you had mentioned, as an aviator, how that fuel tax exemption is handled. It would seem to me to be a very, very logical way in which this could be done. Could you, for the record, just briefly explain to the subcommittee how, as an aviator, it is handled?

Mr. TRUE. Yes; I have a fuel supply on my farm, and I have a tax exemption number supplied to me by the State of Texas. That number is on file with my supplier there locally. When they deliver me fuel, there is no tax applied to me. If we are audited, well, then we are audited through our supplier, and he has the record to make sure that the tax was not collected and was not imposed on me. So, I think a similar method of this could probably be applied to diesel fuel.

Mr. COMBEST. The taxes on the State level. How are those exemptions handled?

Mr. SPANNAUS. I am not aware.

Mr. COMBEST. Are you aware, Mr. True, of how those are handled on a State level?

Mr. TRUE. On diesel fuel?

Mr. COMBEST. Yes.

Mr. TRUE. No; I am not, Larry. I am really not.

Mr. COMBEST. There is a likening that it is handled exactly the way your aviation fuel exemption is. I contemplate that would be another option. What I would like to be able to do is present some options to the Internal Revenue to see if they agree that such proposals could be implemented. I used to be in a wholesale business. You would sell to a tax-exempt retail store that did not have to pay sales tax if that individual had that sales tax number, such as you have for aviation fuel.

Mr. Hutter, in addition to growing up on a farm, my family did not call ourselves oil marketers, we were in wholesale oil business. We had a small wholesale oil business and had to service several service stations and a few truck lines and a lot of farmers. I can appreciate some of the problems that you are going through. A few weeks ago, I presume, when you were in town earlier, a number of oil marketers from Texas came by to visit with me.

Mr. HUTTER. Yes.

Mr. COMBEST. They brought up a problem that I had not really thought of at the time, but I think it is something that bears repeating because it, I think, exemplifies again that this is very, very far reaching.

In your cash-flow problems, whether you bill out on a 30-day basis or not, you are going to have to deal with that tax. That is going to create a cash-flow problem. If you are dealing with farmers, as you have indicated, most people who are in agricultural areas understand that agriculture accounts are not always billed on a 30-day basis. Payment is based on when the crop comes and hopefully it will come in.

In addition, they brought up another point to me that I thought was very interesting.

Another group—I wish Mr. Martinez was still here, because he said he was not that terribly familiar with agriculture—that is affected is municipalities and those who are normally tax exempt. Now, it was my understanding from those oil marketers who had visited my office that a refiner, at his location of purchasing fuel, could exempt to a municipality where you could not.

Mr. HUTTER. Yes; I could. If the refiner does not agree to give me my money back, I am out.

Mr. COMBEST. If the refiner does not make that agreement.

Mr. HUTTER. Right.

Mr. COMBEST. Sorry. I should have finished that statement. Their concern was that municipalities, obviously because of the fact that they are dealing with their cash-flow through taxes, because the local taxes that they raise, are not going to pay an additional tax, would go to the refiner directly, therefore, bypassing the wholesaler.

Mr. HUTTER. Absolutely.

Mr. COMBEST. Or oil marketer and, therefore, you lose a substantial customer.

Mr. HUTTER. You have an accurate understanding.

Mr. COMBEST. I thought it was very interesting because that had not come to our attention before. So, the intricacies of this thing are beyond just what is primarily on the surface. I think that is one of the reasons that we have, again, like today on my bill, 93 cosponsors and many, many others on other bills. My cosponsors represent 35 States. I think it shows the magnitude of the bill and of the problem.

I, with you, hope we can do something about it. Thank you, Mr. Chairman.

Mr. HUTTER. May I respond to a question you asked about the tax collection? In the State of Illinois, in order for a customer to buy diesel fuel for highway use, they must have a bulk user number, a BU number. We register them. If that same customer wants to buy diesel fuel or a distillate—and when I say, "distillate," I am talking about No. 2 heating oil, kerosene, anything that could be burned in a diesel engine—if they want to buy it tax-free, they must provide an affidavit.

Our responsibility is to do it. We have to secure it because if our customer bamboozles us—you know that meaning—and there is a tax levy against that guy, they do not deal with that farmer or customer, they deal with Hutter. I have to pay it. Then I have to go back and get it from the customer. So, we make every effort in the world to have every one of our customers properly registered.

Now, in Illinois, the Illinois Revenue Department is able to audit, does audit, and audits accurately. I am not totally familiar. I have been there a time or two. They are computerized. I suggested to our board of directors of the PMAA that if the IRS has a real problem on this, we ought to finance for them a computer that is tied into every State in the union, and they do not have to go out and audit. They can just pull it in off the wire because Illinois does it beautifully. I am certain many other States do, too.

The young lady is shaking her head yes, behind you.

Mr. COMBEST. Texas does it extremely well. That was the point I was getting to and never finished up after I had asked the question. Texas does it extremely well, as well, and the people in the business have no complaint with the comptroller in the State of Texas.

Mr. HUTTER. That is why it is so frustrating to tell us that it cannot be done. We are audited at the State level. I can tell you an instance where we had a 55-gallon distillate charge and the 55 gallons of product went into a barrel, and it was kerosene that was for a water heater to keep the water trough for the hogs from freezing. That is how accurately they audited. Sure, when we told them what it was, they dropped it, but that is how closely it is audited.

So, I will not accept that a taxing body cannot audit properly, and I do not think you will either.

Chairman HATCHER. Well, gentlemen, you have helped the cause by being here today and by testifying. There is one other way you can help, and you have probably already done this, but anybody in the room, contact Members who have not signed onto one of these bills, and, if they represent you in the House or the Senate, let them know how you feel about it. If we get enough people, we are

going to get this thing passed. Maybe not by April 1, but soon. Thank you very much for being here.

Mr. HUTTER. Thank you, Mr. Chairman.

Chairman HATCHER. The next panel is comprised of Mr. Richard Lewis, vice president of American Pulpwood Association; Mr. Howard Menaker, general counsel, National Association of Truck Stop Operators; and Mr. Frank E. Willis, chairman, Willis Construction Co., who is appearing on behalf of the Associated General Contractors of America.

Chairman HATCHER. Is that Mr. Menaker? How do you pronounce that?

Mr. MENAKER. Menaker.

Chairman HATCHER. Unless you, gentlemen, have another preference, we will proceed in the order in which your names were called and hold questions until the end of the testimony of the three of you. Is that OK?

Mr. LEWIS. That will be fine.

Chairman HATCHER. We will begin with Mr. Lewis.

TESTIMONY OF RICHARD LEWIS, VICE PRESIDENT, AMERICAN PULPWOOD ASSOCIATION

Mr. LEWIS. Thank you, Mr. Chairman.

I know time is growing short but let me say that nobody here, yet, has spoken for the community that involves forestry and the independent logging contractors that serve this Nation's pulp and papermills and sawmills. These logging contractors buy offroad diesel fuel that is used in the felling of trees, the skidding of these trees out to a roadside location, and the processing and loading of these trees on highway trucks.

Our numbers are not as big as some of the other numbers in the agricultural community, although we feel we are part of it. But if the IRS starts collecting this 15-cents-a-gallon tax on offroad fuel on April 1, the Nation's logging contractors, as a whole, will end up coughing up approximately $68 million each year and then have to file for a refund or a tax credit to get their money back.

The impact of the collection of this offroad diesel fuel tax on the individuals is significant, and we have gathered some data that is attached to my statement. I would draw attention to two logging contractors from your State. I am not sure if they are in your constituency or not, Mr. Chairman, but Mr. Ray Hunt, in Omega, GA, has one crew, and he has some equipment you see listed, and he uses about 22,500 gallons a year. Starting April 1, he will not be able to qualify for the $1,000 quarterly rebate so he is going to have to pay another $3,375 and nobody knows how long it is going to take him to get that back from IRS. I do not think it is going to be 12 months. It is probably going to be 14, at least, minimum.

One of our largest logging contractors who was here with me, today, but had to leave, has just been appointed to the Federal Reserve Board in his area. He has a different situation in Michigan. He is going to have to lay out $32,700 each year. Then we have Deck Trevitt Logging in Forsyth, GA. He is using with two crews about 57,000 gals a year and his negative cash-flow impact is going to be $8,550.

Like all the others before me, just let me say on behalf of these logging contractors, that what IRS is proposing—collecting this money and refunding it to them sometime in the future amounts to what we think is an interest-free loan and an unacceptable practice.

We are in support of Mr. Combest's bill and also Mr. de la Garza's bill which would permit the tax-free sales of diesel fuel use offroad. We encourage all the other sponsors of bills who have limited their bills to just agriculture to consider broadening it to include others who are going to be affected.

We do not have, in our analysis, quantification of how much offroad fuel is used by other members of our association, the Nation's pulp and paper companies when they carry out reforestation practices on their lands, when they build roads, and when they site prepare lands to regrow new forest crops. But we feel that is going to be at the very minimum another 100 million gallons and another $15 million cash-flow effect.

We are also disappointed that the IRS is not here to hear what we all have to say. I am absolutely puzzled by it. I figured you would have a whole panel of IRS folks. I guess what I would like to say is: Please do not forget the logging contractors. We will support your bills and will do what is necessary to help to work for passage of them. Thank you.

[Mr. Lewis' prepared statement, with attachments, may be found in the appendix.]

Chairman HATCHER. Thank you. Mr. Hunt is in my district. I do not know him. I wish you would tell him I am looking after his interests.

Mr. LEWIS. I will be glad to.

Chairman HATCHER. Mr. Menaker.

TESTIMONY OF HOWARD MENAKER, GENERAL COUNSEL, NATIONAL ASSOCIATION OF TRUCK STOP OPERATORS [NATSO]

Mr. MENAKER. Thank you, Mr. Chairman, and Mr. Combest.

I, too, will be brief today. As you know, Mr. Hatcher, because we have testified before you before, and Mr. Combest, I am sure you know, the National Association of Truck Stop Operators represents the majority of the full service truck stops in the country.

As pertains to this hearing, particularly, it is important to remember that truck stops sell some two-thirds of all the diesel fuel marketed in the United States. That is a combination of both on and offroad uses. At the moment they are the tax collectors for the IRS for those uses which are taxable.

We support the concept of restoring the exemption from the Federal excise tax to farmers and other off-the-road users, but would be careful to illustrate to you, and would like to work with you on a problem that restoring that exemption by itself would create.

We know that there were problems before in terms of collection of the diesel tax. We understand that those happened, and, in fact, NATSO offered on many occasions to work with the IRS to improve enforcement of the tax laws.

But the good intentions of the Congress in the late days of last session, as we all now know, went somewhat awry. The good inten-

tion was to collect more tax. The good intention was to make sure that there was more revenue for the Government.

But this burdensome credit and refund system which was passed in those late hours in December clearly, as everyone has said today, allows the Federal Government to use money that the farmer is paying, but does not owe.

Again, we share a common goal. But, if we restore that exemption to farmers, loggers, and other off-the-road users without moving the point of collection of that tax back to the retail sale, then we have only shifted that burden. We have only created a whole new set of problems. There is, in fact, very little way to accurately determine the end use of diesel fuel, of that product, at any point in the production or the distribution cycle except at the point of final sale. It is virtually impossible to tell at any point further up the chain whether that it is going to be for on-the-road or off-the-road use. For some retailers who only sell off the road, that may be possible. But for retailers who sell both onroad and offroad uses, there simply is no way to tell at the time it is purchased from the wholesale distributor.

If the taxable status, whether it is tax-free or taxable fuel, is determined by the ultimate use, then that determination has to happen at the time of retail sale. I would contend and hope you would agree that, therefore, the determination and the collection of that tax can only happen at that point.

If we do not move the point of collection back to the retail sale, then there are two alternatives, and I think they are alternatives that both of you would agree are not terribly attractive. The first one is that you restore the exemption to the farmer and other off-road users. He does not pay the tax at the time that he purchases from the retail distributor. However, the retailer, under the current law still has to pay that tax at the time that he purchases the product from the wholesale distributor. So, what have we done?

We have shifted the same problem that the farmer has now, paying a tax he does not owe, and we have shifted it to another small businessman, the truck stop operator. This is not exactly a solution that I think either of you or any of us would like to see.

The other alternative is that we try to avoid that problem somehow by allowing a retailer to estimate how much offroad fuel he is going to sell or how much over-the-road fuel he is going to sell. Well, this invites incorrect reporting which is exactly what we are trying to avoid. Or, in fact, some cases of evasion. I would agree with all those witnesses who have said that the evasion caused by off-the-road use was very minimal. But there are those people who want to avoid paying the taxes. They will then buy it from the wholesale distributor, and say, "Well, the bulk of this is for off-the-road use." And there is nothing to assure that at a later date they do not pump that into a truck going across the road.

So, the attempt of the Budget Reconciliation Act and the provisions on diesel last year, and our goal today, has to be reducing evasion, closing loopholes. and producing better enforcement. We will continue to work with you, and we will continue to reach the conclusion that if the exemption on off-the-road use is restored—and, in fact, it should be—that the collection of the tax at the retail level has to be restored at the same time.

There are only 28 days, we all know, to the implementation date for these changes, and while I join every other witness in hoping that we can do something in those 28 days, I know the realities of Capitol Hill. But let's not try and rush through simply a restoration of the exemption because that will solve some problems. Indeed, it will, but it will create others.

In light of that fact and in quick summary, I would say again that the National Association of Truck Stop Operators stands ready to work with the two of you, with the other cosponsors, with the other authors of different pieces of legislation to see that we do not create more problems as we try and straighten out this mess as best as possible. Thank you.

[Mr. Menaker's prepared statement may be found in the appendix.]

Chairman HATCHER. Thank you, Mr. Menaker. Mr. Willis.

TESTIMONY OF FRANK WILLIS, CHAIRMAN, WILLIS CONSTRUCTION CO., ON BEHALF OF THE ASSOCIATED GENERAL CONTRACTORS OF AMERICA [AGC], ACCOMPANIED BY PAUL LUKENS, AGC HIGHWAY DIVISION MANAGER

Mr. WILLIS. Mr. Chairman and Mr. Combest, thank you for the opportunity to be here and talk to you about the construction industry this morning.

My name is Frank Willis. I am chairman of Willis Construction Co., a highway construction firm in Florence, SC. I am also a member and a national director of the Associated General Contractors of America, a national trade association, representing over 32,000 of this Nation's leading general contracting construction firms and affiliated businesses.

I am accompanied here today by David Lukens, who is an AGC highway division manager. I am pleased to appear before you to have the opportunity to discuss the adverse effects on the construction industry of the repeal of the upfront diesel fuels excise tax exemption. AGC most appreciates the subcommittee's willingness to examine this issue and appreciates the opportunity to present our views to the subcommittee.

Mr. Chairman, as an industry comprised mainly of small businesses, the repeal of the upfront diesel fuels tax exemption comes as a special hardship to construction. We in construction—and construction as an industry is a highly energy intensive industry—consume large quantities of diesel fuel in offhighway uses such as earth moving for highway and dam projects, and fueling asphalt hot-mix plants, and paving equipment.

We are talking about equipment here such as bulldozers, motor graders, heavy scrapers that obviously are not and cannot be used on highway facilities. Since the diesel fuels tax is a user fee, assessed on highway users to pay their share of the construction and rehabilitation cost of the Nation's highway system, offhighway uses have rightly been exempt from the tax in the past. The repeal of the upfront exemption may at first seem like a small change in the law. However, that change brings some major cash-flow management problems to my construction industry.

To give you some insight into the problem from the construction industry standpoint, let me highlight a number of the aspects of this change that are particularly troubling to our industry.

First, it is important to consider the quantity of diesel fuel that even a typical small contractor uses in offhighway construction. AGC conducted a survey in December to determine the impact of the tax change. The results indicated that small highway contractors on the average used 200,000 to 300,000 gallons of diesel fuel each year in offhighway activities. Small- to medium-sized asphalt paving contractors used 600,000 to 700,000 gallons of fuel each year. One of our largest contractors who constructs major dams in this country uses up to 8 million gallons of diesel fuel in 1 year.

At 15 cents per gallon, the cash-flow implications of the tax change are obviously very significant to these contractors. For that average highway contractor using 200,000 to 300,000 gallons of diesel fuel each year that firm will carry an additional $30,000 to $45,000 annual cash-flow burden.

The asphalt paving contractor will carry an additional $90,000 to $105,000 a year cash-flow burden. The large contractor will carry an additional $1.2 million in cash-flow burden.

Obviously, for small, medium, and large contractors, these are sizable sums of cash that these contractors will now have to pay the Federal Government up-front.

Second, we understand that the Treasury is contemplating a quarterly refund process for refunds of $1,000 or greater and an annual process for other sums. Anticipating that there will be a flood of refund applications, we expect that there will be a delay, and most likely a lengthy delay, in processing refund checks. All without interest for the Government's use of our money.

Third, construction contracts are often long term in nature and at a fixed price. Since the tax change will significantly increase the price of fuels on existing contracts, it is retroactive to us as it becomes law. The construction industry then will have to absorb these increases into already agreed upon contract prices.

The AGC recognizes and fully supports the desire of Congress to close loopholes in the tax system which permit the unscrupulous to evade payment of taxes they rightfully owe. We have a hard time understanding, however, the fairness of a tax provision which requires individuals to pay tax for a legitimate nontaxable activity and then apply for a refund which they hopefully will receive sometime in the future without interest. Combined with all the other tax accounting changes that the construction has faced in the last 2 years, we have to say: "Enough is enough."

Since the enactment of the exemption repeal provision in December, construction, agriculture, and other industries have been seeking a remedy to the situation. In response, a number of bills have been introduced addressing different industries' concerns. In the House, H.R. 3685 sponsored by Congressman Combest—and we certainly appreciate your help, Congressman—with some 90 cosponsors—we are delighted to hear that—restores the exemption for agriculture and most other offhighway uses.

In terms of equity, this is the fairest approach. As you are undoubtedly aware, four categories of diesel fuel users were specifically mentioned in the exemption repeal provision. Diesel trains, non-

commercial aviation, nonmotor industrial users, and State and local Governments. The Treasury is authorized to screen entities in these four categories on a case-by-case basis and convey tax-exempt status to them provided they meet certain requirements documenting the nontaxable use. We understand that provided the IRS has sufficient manpower to screen and audit entities which apply for the upfront exemption, the revenue impacts of this process should be negligible.

I would like to digress a moment and address something we have heard some others talk about today—that is compliance. In South Carolina, for example, the diesel fuel tax is handled in, we think, a most efficient manner. As a contractor in South Carolina, the Tax Commission establishes what our equipment fleet consists of. They then take that equipment that is in that fleet—and in our case this consists only of dump trucks—which are onhighway vehicles. They exempt everything else from the fuel tax. We buy the diesel fuel at the wholesale level. Then we monitor the mileage on our dump trucks each month. There is a formula that has been approved by the Federal and the State tax commission that allows us a rate of 5.5 miles per gallon of fuel that goes in those trucks. We then, at the end of each month, compute the miles that our trucks have driven, write the check for that tax, and deposit it the first of the month in the bank directly to the Federal Government. They have their tax money promptly, and I think that is pretty quick pay. It works very well. South Carolina Tax Commissions also performs audits, and we think they have a very workable method for following the procedure and collecting their tax and avoiding any fraudulent activities.

The AGC believes that if this process that is outlined in the previous testimony is fair for the other four categories of diesel fuel users, then the process should be extended to other qualified offhighway business uses. We fail to see the equity in limiting the opportunity to seek the exemption to some types of industries while excluding others who have an equal claim to the exemption.

As an industry, construction will stand toe-to-toe with agriculture, aviation, and any other qualified offhighway user of diesel fuel. Upon examination, AGC believes that the subcommittee will fail to distinguish any reasonable difference in the legitimacy of construction's nontaxable status compared with those of other qualified offhighway uses.

In closing, Mr. Chairman, AGC urges the Congress to act quickly to address the inequity of the repeal of the diesel fuel tax exemption for all industries which have legitimate nontaxable uses. April 1 is almost upon us. Again, AGC appreciates this subcommittee's desire to examine the issue. We look forward to working with you as a subcommittee, and we thank you for your promptness in holding hearings that will allow us to address the issue.

[Mr. Willis' prepared statement may be found in the appendix.]

Chairman HATCHER. Thank you, Mr. Willis.

Mr. Combest, do you have questions of the panel?

Mr. COMBEST. Mr. Chairman, I do not. I would just express appreciation to all of you for coming and for your help.

Chairman HATCHER. Thank you, and do not forget to notify your Member of the House and Senate.

Our next and final panel of witnesses does consist of Mr. Bob Nash, who is president of the Georgia Farm Bureau. I certainly appreciate your being here, Bob, and welcome to you. Mr. Jim Reid, who lives just outside the congressional district I represent, and the only constituent I have here; and Mr. R.D. "Buck" Grist, Jr., from Grist Oil Co. in Blakely, GA. I believe you are representing the Georgia Oilman's Association, too. Is that right?

Mr. GRIST. That is right.

Chairman HATCHER. If you do not have any objection, gentlemen, we will proceed in the order in which your name was called and delay questions until after all you have testified. Is that OK with you? OK, Bob.

TESTIMONY OF ROBERT L. NASH, PRESIDENT, GEORGIA FARM BUREAU FEDERATION

Mr. NASH. Thank you, Mr. Chairman, and Congressman Combest. We appreciate the opportunity to be here and to address these remarks to the subcommittee. Thank you for the opportunity to speak on behalf of 170,000 Farm Bureau members in the State and a large part of our industry in Georgia. The largest industry we have is agriculture.

The provision of the Omnibus Budget Reconciliation Act of 1987 which changed the collection point of diesel fuel tax from the retail to the wholesale level will create a very serious problem for Georgia farmers and those in agriculture throughout the Nation.

We question, as an unfair practice, the intent of Congress to raise revenue for the current fiscal year and refund it the next year. We feel that there is no justification for this change when farmers are trying to recover from low-income years and low-market prices.

It is possible that the intent of this legislation was to prevent violations of offroad purchase of fuel used in onroad vehicles. However, there are presently State and Federal laws which control the use of offroad purchases of fuel. This area is well-regulated and monitored with monthly and quarterly reporting and payment of fuel taxes. We feel that there is no justification for enacting this legislation with the intent of finding violators.

The fact that Congress continues to exempt offroad use from the excise tax provides further proof that the intent of legislation was merely to provide a vehicle to collect revenue for budget-balancing purposes. However, the statute provides the Secretary of Treasury with the authority to exempt certain uses such as diesel-powered trains, commercial aviation, and State and local governments. We feel that agriculture, as a large user of diesel fuel, deserves the same discretionary exemption.

This new burdensome law would cause cash-flow problems for farmers and would also result in higher interest costs. The latest available statistics show that in 1982, which is the U.S. Census time, Georgia farmers used approximately 62,162,162 gallons of diesel fuel. Using this same estimate figure for 1987 and multiplying by 15.1 cents per gallon which farmers will pay as a result of the new legislation results in a total of $9,386,486 in capital outlay which the Government will be holding for Georgia farmers, alone.

With a 12-percent interest rate considered because of the need of farmers to secure additional operating loans, this legislation could cost the Georgia farmers an additional $1,126,378 in interest. Because farmers are exempt from diesel fuel tax on offhighway use, it seemed illogical to force them to pay a tax and then file for a refund or a tax credit.

Agriculture is a high user of short-term production credit. Many farmers secure their loans from governmental or quasi-governmental agencies such as Farm Home Administration and the Farm Credit System. With this new legislation, the Federal Government would not only be provided an interest-free loan from the farmers, but would also force the farmers to pay additional interest to the Government on operating loans borrowed through these agencies.

Most farmers in Georgia probably would not qualify for the quarterly refund requirements of $1,000 or more and would be required to wait until the end of the tax year to file for the refund or a tax credit. Many farmers may not have a taxable income against which that credit could be applied.

Mr. Chairman, and members of the subcommittee, Georgia farmers are beginning to see a slight upturn in agricultural economy in our State. However, we are in no position to provide interest-free financing to the Federal Government, especially on a tax we do not owe.

At this critical time, Georgia farmers need every available penny to continue rebounding from the agriculture crisis that has been upon us in the past years. We find it ironic that the Federal Government has developed seminars to educate small businessmen and farmers in methods of reducing debt obligation and then essentially generate more debt obligation through the enactment of this burdensome new law.

The Farm Bureau has long been an advocate of less Government spending. In addition to what it costs the farmers from bookkeeping and high interest costs, the Government itself will incur more expenses because of the refund process.

It is impossible to know exactly how much this entire process will cost the American taxpayer. We believe it is fitting that the Subcommittee on Energy and Agriculture of this Committee of Small Business is probing the critical issue. Farmers are small and large business people, just the same as those on Main Street. It is important for farmers to be able to meet their debt obligations just as it is important for any other business person. This new law would severely delay the ability of farmers to meet that debt obligation.

As you are aware, several bills have been introduced to eliminate the impending problem. We appreciate the support of the members of this subcommittee who are sponsors and cosponsors of pending bills. We especially thank you for holding the hearing today, and we trust that Congress will take action to correct this unjustified legislation before it takes effect on April 1. I appreciate it very much being with you today.

[Mr. Nash's prepared statement may be found in the appendix.]

Chairman HATCHER. Thank you, Mr. Nash. Mr. Reid.

TESTIMONY OF JIM REID, FARMER, AMERICUS, GA

Mr. REID. Mr. Chairman and Mr. Combest, I am Jim Reid. I live and farm in the Shiloh Community of Sumter County, GA. I serve on the Sumter County Farm Bureau Board of Directors and also on the Georgia Farm Bureau Peanut Advisory Committee. My brother, William, and I farm 1,700 acres scattered across our home county. We raise peanuts, corn, cotton, wheat, and soybeans.

I come here today to share with this subcommittee my concerns as a farmer over the burdensome and troublesome provisions of the Omnibus Budget Reconciliation Act of 1987 which changes the point of collection for the diesel fuel tax from the retail to the wholesale level.

In 1987, we used 39,835 gallons of fuel in our tractors and irrigation engines. We expect to use at least this much, and probably more, in 1988. If the 15.1 cent tax had been applied to agricultural fuel last year, we would have expended $6,015.08 in taxes. I feel our circumstances would be a fair representation of farmers in my area.

In preparation for the 1988 crop, we have established our cropping plans and budgets; obtained our line of credit; and pledged our collateral for this line of credit. All these plans were made before we knew anything about this tax. If this tax is actually collected as proposed, we would have to make additional arrangements and provide additional collateral.

I respectfully seek your consideration of legislation that would allow farmers to continue to buy fuel without prepaying the tax if it is used for offhighway purposes. I base this request on the following points:

First, agriculture which uses the fuel for offroad purposes is not required to pay the tax. It is a road-use tax. I might add though that we pay a lot of road-use taxes indirectly in the way of freight charges on the products we buy, produce, and sell.

Second, I will have to pay interest on the money I borrow to pay the tax, but only be reimbursed for the tax paid. I possibly will have to wait from 5 to 18 months for a refund. I am not in the business of interest-free financing of anyone, much less the Government. I do not believe I should be forced to do so.

Third, since I would have to pledge collateral for the line of credit, I would be denied the use of this collateral for crop production. Using the sum previously mentioned, I could finance the production of 32 acres of corn, 21 acres of cotton, or 15 acres of peanuts.

Fourth, it will increase cost due to the increased paperwork. It would begin with my wholesale supplier, which he would pass on to me. The Government will have to hire additional staff to handle the paperwork. It makes very little sense to pay staff to handle paperwork on a tax that was not owed to begin with. In my opinion, it is simply a waste of time and money.

Fifth, it has been pointed out that some will fail to apply for their refund due to the paperwork required. If this is the case, the tax dollars would be obtained deceitfully. I do not care how you camouflage or rationalize this type of tax collection, it is wrong.

Gentlemen, as a farmer, small businessman, and taxpayer, I hope you will take immediate action to correct this ill-conceived notion. The tax is an unwarranted burden on agriculture. It is a waste of public and private time and money. If this tax was needed to reduce the Federal deficit, I request that you repeal this burden and seek ways to reduce Federal spending.

I thank you for your time and the opportunity to participate in our system of government. Good day.

Chairman HATCHER. Thank you, sir, for your testimony. Buck, we will hear from you next.

TESTIMONY OF RICHARD GRIST, GRIST OIL CO., BLAKELY, GA, REPRESENTING GEORGIA OILMEN'S ASSOCIATION [GOA]

Mr. GRIST. Mr. Chairman, members of the subcommittee, I appreciate the opportunity to testify before you, today. I am Richard Grist. I am from Blakely, GA, and I am in the petroleum marketing business, and I am also a farmer. Today, I am representing the Georgia Oilman's Association.

The Georgia Oilman's Association is composed of 340 small businessmen in Georgia that market gasoline, diesel fuels, oils, and other petroleum products. Today, I would like to stress upon you the impact that the Budget Reconciliation Act passed by Congress will have on the rural areas of America, especially the ones that are dependent on agriculture and forestry.

The portion of this law that is most disturbing to us is, of course, the one we have discussed today that would cause us to have to charge our farmers, foresters, pulpwooders, loggists, the 15.1-cents-a-gallon tax on diesel fuel. We feel like it is wrong to have to charge them this tax. They do not owe the tax. We do not feel like they ought to have to pay that tax. But that is just the beginning of just a whole multitude of problems that come about when we charge this tax.

Speaking from a petroleum marketer's standpoint, nearly all of the diesel fuel we sell farmers is a credit sale. I sell about 2.5 million gallons of diesel fuel a year. Less than 1 percent of that is a c.o.d. transaction.

Now, when we put that 15.1 cents extra on our books that is going to cause our accounts receivable, based on diesel prices today, to go up 20 or 25 percent. Accounts receivable are high enough already. September 1, 1987, my accounts receivable were $368,000. All right. They were $368,000. People are supposed to pay net at 30, but sometimes people just cannot pay net 30, a lot of our accounts cannot.

All right. I had $97,000 of that which was over 30 days' old. Of that $97,000, $36,000 was over 90 days' old. So, you all can see what a problem we have right now of accounts receivable. Now, you add 23 percent more to that and that just makes the problem worse than it already is. It is bad enough as it is.

Now, we talk about a refund. It is nice if farmers could get a refund, but really, they do not have the money up front to pay it, and the recordkeeping is going to really present a problem. Most small businesses and small farmers do not have the bookkeeping

facilities to capture that data daily that is coming in that they would need for their refund at the end of the year.

I know what is going to happen in our business. My customers are going to come to me at the end of the year and say, "Look here, I need to know how many gallons of diesel fuel I bought last year so I can make my refund." I am going to give it to my customers if that be the situation, but it is going to cause me to have to go to a lot of expense.

With my bookkeeping facilities right now, I cannot capture all that daily on my computer. What I would have to do is go back over every invoice and take those gallons down for that particular customer. I have got around 200 farm accounts, and I imagine 150 of them I could safely say would actually come in, and want me to give them this data where they could file for their refund. We already have to do that for AGPOLIS—people that qualify for a refund on gasoline.

In South Georgia, the agricultural economy is bad. Congressman Hatcher can tell you that. He can relate to that real well. He is from South Georgia along with me. There is one oil jobber in Cordale, GA. In the last 4 years, he has had to endure 38 bankruptcies, and this is why it nearly fell out. He has had 38 bankruptcies in the last 4 years. Now, you just imagine, this money he has lost, and you tack 23 percent more onto it, and imagine that he would not be there today.

Another item I would like to bring up that had not been brought out. We have a lot of FHA farmers that farm with us, people who are using FHA for credit. That is the credit of the last resort. From last year's poor crop year, most of these farmers are 2 or 3 months behind paying right now. What they are doing is, they have bought from November up until now, and they are waiting on this operating money to come in to pay for this debt that they have already incurred.

I have talked to our county office and another county office. Of the farmers that are farming with FHA, they say not one of their accounts or clients has added this 23-percent increase in fuel in his budget for the following year. So, that is going to open up another can of worms. Your FHA farmers are going to be running out of money a lot quicker than they have in the past.

I checked with the U.S. Extension Service and their estimate for fuel in Georgia for farmers and forestry to be 100 to 110 million gallons. All right. That 100 to 110 million gallons, when we add the tax onto that, that is going to be roughly $15 million.

All right. We are going to take $15 million out of an economy that is already poor. That is not going to just effect farmers. It is not just going to effect the petroleum man. It is going to effect everybody who lives in rural America in a negative way.

Today, gentlemen, I am here before you, and I ask you to please continue to work hard to try to rectify this inequitable situation that I feel we are faced with right now. I appreciate you allowing me to testify, and I will try to answer any questions you have.

[Mr. Grist's prepared statement may be found in the appendix.]

Chairman HATCHER. Thank you, Buck. I assure you that a lot of other Members are going to push as hard as we can to see that the

situation is corrected. How many Georgia counties do you operate in?

Mr. GRIST. I operate, oh, I do not know, probably 12. I go into Georgia, Florida, and Alabama.

Chairman HATCHER. Well, we do thank each of you for being here.

Do you have questions or comments, Larry?

Mr. COMBEST. Just sort of a related question.

Mr. Reid, farmers fuel their irrigation equipment with diesel fuel in Georgia?

Mr. REID. Yes, sir.

Mr. COMBEST. Exclusively? Or are you talking about light pumps?

Mr. REID. No; we pump out of surface creeks and surface ponds.

Mr. COMBEST. Portable pumps and motors.

Mr. REID. Yes; we have basically John Deere engines. We have one Caterpillar.

Mr. COMBEST. You fuel those with diesel fuel?

Mr. REID. With diesel fuel.

Mr. COMBEST. Mr. Grist, I think sometimes Charlie and those of us around farming think everybody understands. I think a lot of people have a question about how do we identify, how do you identify where the diesel goes? Of those, I believe you said 200 farm customers?

Mr. GRIST. Yes.

Mr. COMBEST. How many of those take delivery on their farm?

Mr. GRIST. I would say 180.

Mr. COMBEST. Nearly all of them.

Mr. GRIST. Yes.

Mr. COMBEST. It is very easy to know when you carry a tank of diesel out, and you put it in, I presume you still provide overhead storage tanks.

Mr. GRIST. Oh, yes.

Mr. COMBEST. That it is easy to know where that is going. That it is not commingled. I think maybe we oversimplify things and just assume people know how this works that when a farmer comes in and buys fuel, they do not really realize that you take it out to him and store it on the farm. You know exactly where it is going and exactly what they use it for. If they are going to use it on the road, they usually buy it in a service station.

Mr. GRIST. Yes, Mr. Combest; another thing, so much of this fuel is used for irrigation. We have exempted heating fuel, and I know you cannot take care of every little thing that comes along, but a lot of this is delivered back into swamps to creeks, rivers, and lakes, and stuff where there is no way there could be any highway use of the fuel.

Mr. COMBEST. Thank you, gentlemen.

Chairman HATCHER. Again, thank all of you for being here. This concludes the hearing.

[Whereupon, at 12:50 p.m., the subcommittee was adjourned, subject to the call of the Chair.]

APPENDIX

OPENING STATEMENT OF CONGRESSMAN HATCHER

GOOD MORNING. I AM CHARLES HATCHER, AND I AM THE CHAIRMAN OF THIS SUBCOMMITTEE ON ENERGY AND AGRICULTURE WHICH IS CONDUCTING THIS HEARING TODAY. I WANT TO THANK YOU FOR YOUR INTEREST IN THIS MATTER AS EVIDENCED BY YOUR PRESENCE HERE TODAY. I WOULD ALSO LIKE TO TAKE THIS TIME TO THANK MY COLLEAGUE, LARRY COMBEST, FOR HIS LEADERSHIP IN ADDRESSING THIS ISSUE.

I WILL KEEP MY OPENING REMARKS VERY BRIEF IN THE INTEREST OF TIME AS WE HAVE A NUMBER OF INDIVIDUALS HERE TODAY WHO WISH TO SHARE THEIR VIEWS WITH US. WITH THAT IN MIND, I MUST ALSO ASK EACH OF YOU WHO TESTIFY TODAY TO PLEASE KEEP YOUR REMARKS BRIEF. WE PLAN TO REVIEW NOT ONLY H.R. 3865, A BILL INTRODUCED MR. COMBEST, BUT THE ENTIRE DIESEL FUEL EXCISE TAX COLLECTION PROCESS. THIS ISSUE HAS DEFINITELY SPARKED INTEREST IN CONGRESS AS EVIDENCED BY 11 HOUSE AND 4 SENATE BILLS. I REGRET THAT WE DO NOT HAVE A REPRESENTATIVE FROM THE INTERNAL REVENUE SERVICE HERE TODAY, SINCE I, LIKE MANY OF YOU HERE, HAVE QUESTIONS OF HOW THEY PLAN TO ADDRESS THIS SUBJECT. THEREFORE I, ALONG WITH THE MEMBERS OF THIS SUBCOMMITTEE, WILL SEND A LIST OF QUESTIONS TO COMMISSIONER LAWRENCE GIBBS OF THE INTERNAL REVENUE SERVICE THAT WE FEEL WOULD HAVE BEEN ASKED OF HIM HAD HE BEEN ABLE TO APPEAR BEFORE US TODAY.

I MUST SAY THIS ISSUE APPEARS TO BE AN EXAMPLE OF AN ACTION TAKEN BY CONGRESS WITHOUT DETERMINING THE CONSEQUENCES OF OUR ACTIONS ON THE SMALL ENTITY. IF THIS PROPOSAL GOES INTO EFFECT ON APRIL 1 AS SCHEDULED, IT WILL WREAK HAVOC ON

MANY FARMERS AND SMALL BUSINESS PERSONS WHO CAN ILL AFFORD TO PAY AN ADDITIONAL 15.1 CENTS ON EVERY GALLON OF DIESEL THEY PURCHASE. THEREFORE, IT IS THE PURPOSE OF THIS HEARING TO SHED LIGHT UPON THIS ISSUE WHICH IS SO IMPORTANT TO MANY OF YOU IN THIS ROOM. I HOPE WE ARE ABLE TO DEVELOP A SOLID RECORD HERE TODAY.

WITH THAT, I WANT TO RECOGNIZE MY COLLEAGUE AND RANKING MINORITY MEMBER, DAVID DREIER, FOR ANY COMMENT HE WOULD LIKE TO MAKE AT THIS TIME.

STATEMENT OF

CONGRESSMAN LARRY COMBEST

(R-TEXAS)

SUBCOMMITTEE ON ENERGY AND AGRICULTURE

COMMITTEEE ON SMALL BUSINESS

MARCH 3, 1988

Mr. Chairman:

I want to begin by commending you for the speed with which you called this hearing. This issue is truly one that has come to the Congress from the grassroots. We have heard an overwhelming cry from farmers and oil field drillers, from tug boat operators and contractors to change this law. I am particularly pleased to welcome my chairman of the Agriculture Committee, Mr. de la Garza, and my Senator from Texas, Mr. Gramm here today to testify on this legislation.

I introduced H.R. 3865 on January 27 to prevent all off road users of diesel fuel from paying a tax they do not owe. Since that time, more than 90 of my colleagues have joined me as cosponsors and the Texas Farm Bureau, Permian Basin Petroleum Association and dozens of other national organization have endorsed my proposal. The message is coming across loud and clear: OUR CONSTITUENTS DEMAND ACTION!!

The newly enacted tax, which will take effect on April 1, just does not make any sense. It will require additional upfront capital from small businesses and farmers least able to afford it. The Internal Revenue Service's use of their money will create a cashflow burden and an unnecessary interest expense on industries which are already experiencing serious economic troubles.

Oil field drillers, farmers, shrimpers, and builders are having a hard time understanding the logic of a law which requires them to pay a tax they do not owe, prove to the government that they do not owe it, then apply to the government for a refund they will hopefully be paid. All this, for a tax we have established should not have been paid in the first place.

In addition, the new law causes serious cash flow problems for industries that are least able to stand it. The collection

point change requires that oil drillers and farmers in my district allow IRS to use their money, interest free, because the agency is doing a poor job of administering present regulation. To explain the serious financial implications of this new law and why it is just bad policy, let me share a few examples from letters I have received from my constituents.

EX. 1 - (SITTON DRILLING CO) - "Sitton Drilling Company operates five drilling rigs which average 500 gallons of diesel fuel per day per rig, or a total of 2,500 gallons per day. This additional tax will cost a total of $377.50 per day, $11,325 per month, $137,787.50 per year.

Quite simply, this is a tax up front that will result higher interest costs and cash flow problems, and additional paperwork and headaches when filing for a tax refund."

EX. 2 - (Lewis Block, farmer) -"This [tax] will result in my having to borrow another $2200 this year to pay this stupid tax. It is hard enough to borrow money these days without having to put up with this."

EX. 3 - (Yale E. Key, Oil Well Services) -"We have bought fuel tax exempt for years and pay the Federal Tax quarterly on the amount used on public highways. Sixty percent of the average 50,000 gallons we buy each month is tax exempt. This will cause us to pay approximately $4,530 a month or $54,360 a year into the Federal Government that we should not have to pay...During the past three years in our business we have not had a profit and are struggling to keep a positive cash flow. This unnecessary out lay of cash will be devastating to cash flow for our company and our industry."

The IRS wants our constituents to do their job for them. Because they are incapable of enforcing their own collection policy, they are going to ask all users of diesel fuel, liable for the excise tax or not, to police the collection process for them. I believe the Congress wants to make sure that those evading the tax are caught, and I think all members have expressed their willingness to look at alternatives to present procedure. On the other hand, my colleagues and I will not stand for a policy which assumes users of off road diesel fuel are guilty of evasion until the IRS decides they are innocent.

I fully agree with the agency that a need for an improved collection mechanism exists. I further understand that Internal Revenue Service has not been able to collect all excise taxes owed to the trust fund. While my record of support for the Highway Trust Fund speaks for itself, funding for maintenance and safety of our public roadways is not the issue in this debate.

I want to welcome S.M. True, who resides in my district, President of the Texas Farm Bureau. His organization has done a tremendous job bringing this issue into focus and assisting many of us here in our efforts to inform other members of the serious problems associated with this new policy. Also from Texas, and here at my request, Harry Spannaus, of the Permian Basin Petroleum Association, will explain the specific problems the new law creates for the energy industry.

Let me add this final thought. It is particularly appropriate for the Small Business Committee to be the first to hold hearings on this issue. For multi-million dollar corporations, an extra 15 cents a gallon for diesel fuel will not matter that much. But, it could mean the crucial difference for many small businesses in my district and throughout the Nation. Many small businessmen and farmers will be the ones to feel the pinch if we do not find a workable answer. I look forward to working

with all my colleagues to see that we make something happen. I appreciate their support for my bill.

Thank you Mr. Chairman.

STATEMENT OF CONGRESSMAN E (KIKA) DE LA GARZA

Before the Subcommittee on Energy and Agriculture of the Committee on Small Business

March 3, 1988

Mr. Chairman, I appreciate the opportunity to address the Subcommittee on Energy and Agriculture. As the Chairman of the House Committee on Agriculture, I am confronted repeatedly with various problems affecting agricultural producers. When an issue rises that needs to be addressed, I try to move swiftly to get our legislative machinery in gear to resolve the issue. Included in the Omnibus Reconciliation Act of 1987 is a provision that requires the collection of excise tax at the wholesale level on diesel fuel for off-highway use. This diesel tax provision is such an issue.

Diesel fuel is widely used by all agricultural producers, large and small, in their farming operations. It has been estimated that nearly three billion gallons per year of diesel fuel is used on America's farms. If the diesel tax is implemented on April 1, every farmer will be required to pay an excise tax of 15 cents per gallon on his diesel fuel. This payment, resulting in hundreds of millions of dollars, will be required even though farmers have an exemption from this tax. The new provision will require farmers to pay the 15 cents per gallon tax and then apply for a refund. Essentially, they are paying a tax they do not owe. Although the provision is designed to increase tax compliance, and I can understand the difficulty

one encounters in trying to collect taxes, this provision is an ill-conceived attempt to achieve that goal.

There have been many bills introduced that would rectify the problem created by this provision, including H.R. 3866, a bill I introduced on January 26th. I would like to emphasize the fact that I am not wed to any of these bills as the only way to correct this problem. I would support any measure that would provide relief.

In addition, any measure enacted should include not only an exemption for agricultural producers, but also an exemption for other off-highway uses. The diesel fuel tax not only detrimentally affects farmers, but numerous other industries as well. Oil and gas, fishing, and construction, to name a few, are all industries severely affected by this diesel tax provision.

This issue is one of vital importance to all of the industries affected. I have received hundreds of letters concerning this issue, all of which ask for a repeal of the diesel tax.

In closing, I would like to thank you once again for the opportunity to testify. Also, I would like to thank the numerous sponsors of all of the bills that have been introduced to rectify this problem, for their help in providing leadership on this issue. By joining together and building a consensus, we

can gain relief from the financial strain imposed by this provision on all of the affected industries.

JIM JONTZ
5th District, Indiana

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TESTIMONY OF CONGRESSMAN JIM JONTZ
SUBCOMMITTEE ON ENERGY AND AGRICULTURE
COMMITTEE ON SMALL BUSINESS
MARCH 3, 1988

I would like to express my appreciation to you, Chairman Hatcher, and your colleagues for allowing me this opportunity to testify before the Subcommittee on Energy and Agriculture of the Committee on Small Business.

You are to be commended for recognizing the problem that has been created for America's farmers and small businesses by the provision in the Budget Reconciliation Act that can now be found in Section 4093 of the Internal Revenue Code. I hope that the attention created by this hearing will result in a delay of the April 1 implementation date for this provision, and will lay the groundwork for a legislative solution to this problem.

I would also like to recognize the efforts of my colleague, Mr. Combest. The legislation which he has introduced to deal with this problem has received considerable support from his colleagues. Last week Mr. Combest, Mr. Daub, and Mrs. Smith joined me in sending a letter to Chairman Rostenkowski about the problems created by Section 4093.

On the first day of this session of the Congress I introduced H.R. 3850, whose purpose was very straight-forward: to prevent farmers from being required to pay diesel fuel excise taxes on fuel purchased for off-road use. The support given to this bill has been very gratifying. 65 of my colleagues have joined me in cosponsoring this bill, which has been endorsed by every major agricultural organization in America.

What has brought organizations as diverse as the American Agriculture Movement and the American Farm Bureau together is the recognition of the great hardship which section 4093 will cause farmers. It is estimated that America's 1.2 million farmers are going to be unnecessarily charged an annual $420 million in

excise taxes - money which does not, and will never belong to the federal government. And in order for a farmer to get his money back - notice that I said "his money," not the government's - he is going to have to fill out another IRS form.

We're told that the reason behind this new collection system is to reduce tax fraud and to make it easier for the IRS to collect excise taxes. Yet the individual who is cheating on his taxes now will not think twice about filing a false report under this new provision. I am against tax fraud, but I believe that the IRS could devise a system to effectively reduce abuse of the system without penalizing all farmers, the vast majority of whom are honest.

I do not doubt, either, that reducing the number of collection points for diesel excise taxes will make it easier for the IRS to collect these taxes. But is it fair to ask American farmers to pay $420 million in taxes every year simply for the convenience of the IRS?

In a letter sent last week to Lawrence Gibbs, Commissioner of the IRS, I said:

"I find it somewhat ironic that this change was made while at the same time the Internal Revenue Service is trying to convince individual taxpayers to "fine tune" their withholding to match the actual amount of tax owed. As you know, this was one of the major reasons for the adoption of the new W-4 form. However, with this new excise tax requirement, farmers are going to be paying taxes that do not and will never belong to the government. In essence, a vast new tax collection and refund system will have to be created to refund these taxes to America's approximately 1.2 million farmers."

It is notable that last week Commissioner Gibbs told a Ways and Means Subcommittee that changes to the tax code are causing even bigger headaches for taxpayers. And when taxpayers can get through on the telephone to IRS assistance offices, the answers they often get are wrong. Now the IRS is going to require farmers to keep new records, file new forms, and then hope that they get their money back, without any interest.

Very few members of the Congress knew about this provision in the Budget Reconciliation Act. We do know about it now, and if we act quickly, we can spare American farmers and small businesses the problems that will be created by section 4093. I hope that this hearing will lead to a quick resolution of this problem through passage of corrective legislation.

TESTIMONY OF THE HONORABLE CLAUDINE SCHNEIDER BEFORE THE SUBCOMMITTEE ON ENERGY AND AGRICULTURE OF THE COMMITTEE ON SMALL BUSINESS- MARCH 3, 1988.

Thank you, Mr. Chairman. I am pleased to be here before this Subcommittee today, to discuss H.R. 3865, a bill introduced by my colleague from Texas, Mr. Combest, and of which I am a cosponsor. This bill amends the Internal Revenue Code of 1986 and changes the tax-free sales of diesel fuel for non-highway users.

This bill does not seek to create tax loopholes for any sector of the economy. It merely seeks to prevent the imposition of a new, burdensome, paper producing tax collection method which is scheduled to go into effect on April 1. This new regulation was included in the Omnibus Budget Reconciliation Act of 1987, which this Congress passed in the days just before Christmas.

This new filing requirement will create nightmares for many small businesses throughout the United States. But the sector of the economy that I feel would be most affected, and the one that I wish to address today, is the commercial fishing industry.

The commercial fishing industry is a significant component of this nation's economy, bringing $14 billion directly into this nation's economy. This is the only sector of the U.S. economy that has a trade surplus with Japan- $1.1 billion in 1987. Yet the industry is comprised almost exclusively of small businessmen. In the Merchant Marine and Fisheries Committee we have been dealing with the economic problems facing the industry. In just the past two weeks our Committee has addressed the wildly escalating insurance premiums facing the industry, as well as the dumping of contaminated sewage sludge in fishing areas. This is an industry that does not need any more unnecessary burdens.

The new regulation that is to take effect on April 1 requires that fishing vessels, and the other non-highway users, pay a 15.1 cent per gallon excise tax on diesel fuel on a quarterly basis. This money will be deposited in the Highway Trust Fund, which will benefit from the accruing interest, and fishermen will have to wait and apply for a refund. I'm not sure how it works here in Washington, D.C., but in my state of Rhode Island, I have yet to see a fishing boat using a highway!

Many fishermen operate on a very narrow profit margin. Fuel costs are a significant operating expense for fishing vessels, generally comprising 27% of those costs. The loss of a significant of amount of their cash flow, as well as the accruing interest, combined with the increased manhours and costs involved with nonproductive paperwork will drive some fishermen into bankruptcy.

Fuel dealers very often sell fuel to fishing vessels on

credit, until the boats return, sell their catch and have the ready cash to pay for the fuel. With the new 15.1 cent tax, these fuel dealers may require cash up front, or else they will be responsible for temporarily paying the tax. Fishermen also plan in advance for their coming year's budget. The passage of this new requirement during the last week of 1987, after fishermen had their 1988 budgets in place, will render those budgets obsolete and useless.

The nightmare that the fishing industry would face seems endless. In Rhode Island our fishing fleets are made up of relatively small single owner boats. The fishermen on each boat are paid on a per trip basis, based on their share. The more experienced people may have a full share, and the others a half or quarter share. Everyone pools money for expenses, based on their share, which includes fuel costs, food, gear, etc. The profits made from the trip are again distributed to each crewmember based on their share. As a rule these trips vary in length of time, distance traveled, crew onboard, share allotments, fuel used, and profits allotted. These crewmembers will be paying the fuel tax when they leave on a trip, but their refunds will be months away. Allotting the proper refunds, to the proper crewmembers, on a proper per share basis, will require each vessel owner to purchase and maintain a computer system that they can't afford!

I understand that the Internal Revenue Service is not represented at this hearing today. If they were, I would like to have asked them how cost effective they estimate it would be for them to process this new requirement for 130,000 fishing vessels on a quarterly basis?

I urge all of my colleagues on this Committee to support H.R. 3865, and to act before April 1 when this unnecessary and burdensome regulation is scheduled to take effect.

Thank you very much, Mr. Chairman.

AMERICAN FARM BUREAU FEDERATION
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STATEMENT OF THE AMERICAN FARM BUREAU FEDERATION TO THE
HOUSE SMALL BUSINESS COMMITTEE
SUBCOMMITTEE ON ENERGY AND AGRICULTURE
REGARDING COLLECTION OF DIESEL FUEL EXCISE TAXES

March 3, 1988

Presented by S.M. True, Jr., President, Texas Farm Bureau, and Member of the Board of Directors, American Farm Bureau Federation

STATEMENT OF THE AMERICAN FARM BUREAU FEDERATION TO THE
HOUSE SMALL BUSINESS COMMITTEE
SUBCOMMITTEE ON ENERGY AND AGRICULTURE
REGARDING COLLECTION OF DIESEL FUEL EXCISE TAXES

March 3, 1988

Presented by S.M. True, Jr., President, Texas Farm Bureau, and Member of the Board of Directors, American Farm Bureau Federation

Thank you, Mr. Chairman and members of the Subcommittee. My name is S.M. True. I am a farmer and rancher from Plainview, Texas. I operate a medium sized, cotton, wheat, feedgrains and cattle operation. I am President of the Texas Farm Bureau and am representing the American Farm Bureau Federation, the nation's largest organization of farmers and ranchers.

I am here today to share with you Farm Bureau's concern over an obscure provision of the Omnibus Budget Reconciliation Act of 1987 which will have a profound impact on millions of farmers and ranchers. This provision changes the collection point for diesel fuel tax from the retail level to the wholesale level. Beginning April 1 of this year, farmers will be forced to pay a 15-cent per gallon excise tax on diesel fuel and then file for a refund or credit. Farmers now have an excise tax exemption for off-highway uses of diesel fuel.

Today we are asking your favorable consideration of legislation that will permit farmers and ranchers to continue to buy fuel tax-free if it is used for off-highway purposes. If this provision is not changed, farmers and ranchers will be burdened with an additional operating expense which will total hundreds of millions of dollars in diesel fuel excise taxes. Although farmers will be able to apply for refunds of these taxes, cash flow problems and higher interest costs to agricultural producers will undoubtedly result.

Costs to agriculture would be substantial. According to the 1982 Census of Agriculture, annual farm diesel fuel use is approximately 3 billion gallons. At 15 cents per gallon, agricultural producers would be forced to pay approximately $400 million in diesel taxes. In my home state of Texas, the impact to agriculture would be about $30 million. On my farm, which is a fairly typical operation, my off-road diesel fuel consumption per year is approximately 8,346 gallons. This means that I will be forced to pay $1,251.90 in taxes to the Federal Highway Trust Fund for fuel used off the highway, on my farm in the production of crops and livestock. Included in my statement for the record are state farm diesel fuel use figures from the 1982 Census of Agriculture. These statistics dramatize the impact of this new tax on farmers nationwide.

This is a tax that farmers do not owe and should not have to pay. It means that I must borrow additional operating capital and that I will have higher interest costs. It means additional regulation and paperwork to obtain a refund. Timing couldn't be worse. This new expense and regulatory burden will be imposed when farmers must cut expenses and increase efficiency to survive.

Although many of the details of the refund system to be imposed are not yet clear, there may be some major inequities. The Internal Revenue Service has informed us that farmers may file for quarterly refunds if the refund for the quarter is $1,000 or more. This would require diesel fuel use of at least 6,667 gallons per quarter or 26,667 gallons per year. Only the very largest farmers use this much diesel fuel. In checking with USDA's Office of Energy, we have estimated that less than 20,000 farmers would qualify to file quarterly for refunds. Most would have to wait until the end of the tax year to file for a tax credit on IRS Form 1040.

There is another problem. Some farming operations may not have taxable income in a given year against which a credit could be applied. We assume that the credit would be carried forward and that farmers who need the money could not obtain a refund for a tax they do not owe. To make matters worse, no interest would be paid by the I.R.S. In effect, farmers will be making interest free loans to the federal government. We think this is ridiculous. Ironically, the costs to the I.R.S. of distributing and maintaining a refund system may outweigh the benefits of any revenue which may find its way to the Treasury.

Last, we would like to bring to your attention a problem which underscores the need for quick legislative action to restore the previous tax-free purchase method of diesel fuel for off-highway use. An excise tax for off-road diesel fuel could increase fuel costs and disrupt the distribution system. This could occur when farmers and other off-road users "top off" their storage tanks before April 1 to avoid paying the extra 15 cents per gallon. This could create sudden, artificial demand for billions of gallons of diesel fuel which could not be supplied by the current refining and distribution system. This problem could be especially serious since it would take place in the early spring, the peak fuel use period for spring planting. Additional strong demand will also exist during the same period for home heating oil, which is essentially the same product as diesel fuel. Higher diesel fuel prices and regional shortages could result.

Mr. Chairman and members of the Subcommittee, the new requirement for collection of farm diesel fuel taxes is unfair, it is of questionable benefit to the federal government, and it will create a new financial and regulatory burden on farmers and ranchers. It will increase production costs and may cause serious disruptions in fuel supplies which are essential in the production of agricultural commodities.

These concerns are shared by fifteen other major organizations which have cosigned a letter to all members of the House and Senate expressing the need for immediate action. I have included that letter for the record as part of my statement.

87-359 0 - 88 - 3

Several bills which would accomplish our objective have been introduced. Although the language of these bills is different to some extent, it is our understanding that each would restore the tax-free purchase of diesel fuel used off the road in the production of agricultural commodities. These bills include H.R. 3844 introduced by Representatives Hal Daub and Byron Dorgan, H.R. 3850 introduced by Representative Jim Jontz, H.R. 3865 by Representative Larry Combest, H.R. 3866 by Representative Kika de la Garza, H.R. 3881 by Representative Virginia Smith and H.R. 3985 by Representative Jamie Whitten. Individual cosponsors of these bills now total more than 130. We commend these members of the House for their leadership in dealing with this important problem and urge your swift, favorable consideration of these bills. The April 1 implementation date is quickly approaching.

Thank you.

TESTIMONY BY

HARRY A. SPANNAUS

EXECUTIVE VICE PRESIDENT, PERMIAN BASIN PETROLEUM ASSOCIATION

P. O. BOX 132

MIDLAND, TEXAS 79702

BEFORE THE

UNITED STATES HOUSE OF REPRESENTATIVES

COMMITTEE ON SMALL BUSINESS

SUBCOMMITTEE ON ENERGY AND AGRICULTURE

THE HONORABLE CHARLES HATCHER, CHAIRMAN

TESTIMONY BY

HARRY A. SPANNAUS

BEFORE THE COMMITTEE ON SMALL BUSINESS
SUBCOMMITTEE ON ENERGY AND AGRICULTURE

MARCH 3, 1988

A B S T R A C T

TESTIMONY IS OFFERED BY THE PERMIAN BASIN PETROLEUM ASSOCIATION, A PETROLEUM INDUSTRY TRADE ASSOCIATION LOCATED IN WEST TEXAS AND SOUTHEASTERN NEW MEXICO AND OTHER INDUSTRY RELATED ASSOCIATIONS NAMELY, THE TEXAS INDEPENDENT PRODUCERS AND ROYALTY OWNERS ASSOCIATION, THE KANSAS INDEPENDENT OIL AND GAS ASSOCIATION, THE NORTH TEXAS OIL AND GAS ASSOCIATION, THE WEST CENTRAL TEXAS OIL AND GAS ASSOCIATION, THE EAST TEXAS PRODUCERS AND ROYALTY OWNERS ASSOCIATION, THE PANHANDLE PRODUCERS AND ROYALTY OWNERS ASSOCIATION, THE COASTAL OIL AND GAS ASSOCIATION AND THE INDEPENDENT PETROLEUM ASSOCIATION OF NEW MEXICO.

WE BELIEVE THAT THE NEW TAXING REQUIREMENTS ON OFF-ROAD DIESEL FUEL AS REQUIRED BY THE OMNIBUS BUDGET RECONCILIATION ACT OF 1987, IS UNJUST AND UNFAIR TO ALL LEGITIMENT USERS OF OFF-ROAD FUELS. IT POSES AN ADDED CASH FLOW BURDEN ON DIESEL FUEL USERS, IT CREATES ADDITIONAL ADMINISTRATIVE EXPENSES FOR BOTH THE USER AND THE IRS IN COMPLIANCE AND VALIDATION AND IT IS A TAX ONLY TO HELP CLOSE ALLEDGED WIDE-SPREAD EVASION OF DIESEL FUEL TAX PAYMENTS TO THE FEDERAL GOVERNMENT WHICH HAS LITTLE IF ANY RELATIONSHIP WITH THE PETROLEUM INDUSTRY OPERATORS OF DIESEL EQUIPMENT.

THE NATION'S DOMESTIC PETROLEUM INDUSTRY IS ATTEMPTING AN ECONOMIC RECOVERY FROM SEVERELY DEPRESSED TIMES. THE FEDERAL GOVERNMENT SHOULD ENHANCE THIS RECOVERY THROUGH FAIR AND JUST LEGISLATION. WE BELIEVE THAT THE NEW TAX REQUIREMENTS ON OFF-ROAD DIESEL FUEL IS CONTRARY TO THIS PHILOSOPHY AND THAT THE LAWS ENACTMENT WILL BE A FURTHER BLOW TO AN INDUSTRY THAT IS ALREADY ON ITS KNEES AND STRUGGLING FOR RECOVERY.

CHAIRMAN HATCHER AND COMMITTEE MEMBERS

THANK YOU FOR THE OPPORTUNITY TO APPEAR BEFORE YOU TODAY. MY NAME IS HARRY SPANNAUS AND I AM EMPLOYED BY THE PERMIAN BASIN PETROLEUM ASSOCIATION AS ITS EXECUTIVE VICE PRESIDENT WITH HEADQUARTERS IN MIDLAND, TEXAS.

THE PERMIAN BASIN PETROLEUM ASSOCIATION HAS OVER 1,300 MEMBERS, COMPOSED OF BOTH MAJOR OIL COMPANIES AND SMALL INDEPENDENT OIL AND GAS PRODUCERS AND RELATED SERVICE AND SUPPLY INDUSTRY MEMBERS, SUCH AS DRILLING CONTRACTORS. THE PERMIAN BASIN IS THE LARGEST SINGLE CRUDE OIL AND NATURAL GAS PRODUCING REGION IN THE LOWER 48 STATES BOTH IN SIZE AND IN PRODUCTION. IT ENCOMPASSES 54 COUNTIES IN WEST TEXAS AND 4 COUNTIES IN NEW MEXICO COVERING OVER 100,000 SQUARE MILES AND IT PRODUCES APPROXIMATELY 23 PERCENT OF THE NATION'S DOMESTIC CRUDE OIL AND 15 PERCENT OF ITS NATURAL GAS.

I AM ALSO TESTIFYING ON BEHALF OF THE TEXAS INDEPENDENT PRODUCERS AND ROYALTY OWNERS ASSOCIATION, THE KANSAS INDEPENDENT OIL AND GAS ASSOCIATION, THE NORTH TEXAS OIL AND GAS ASSOCIATION, THE INDEPENDENT PETROLEUM ASSOCIATION OF NEW MEXICO, THE WEST CENTRAL TEXAS OIL AND GAS ASSOCIATION, THE EAST TEXAS PRODUCERS AND ROYALTY OWNERS ASSOCIATION, THE PANHANDLE PRODUCERS AND ROYALTY OWNERS ASSOCIATION, AND THE COASTAL OIL AND GAS ASSOCIATION, WHOSE COMBINED MEMBERSHIP IS IN EXCESSIVE OF 10 THOUSAND MEMBERS WITH COMPOSITIONS LIKE THAT OF MY ASSOCIATION.

WE COMMEND THIS COMMITTEE FOR CONDUCTING THIS HEARING TODAY. WE BELIEVE IT IS IMPORTANT IN THIS TIME OF DOMESTIC PETROLEUM INDUSTRY DEPRESSION TO TAKE WHATEVER MEASURES THAT ARE REASONABLE AND NECESSARY TO PROVIDE FAIR AND JUST TAXATION TREATMENT TO AN INDUSTRY THAT IS ALREADY ON ITS KNEES AND FIGHTING FOR RECOVERY.

THE NEW LAW TO COLLECT "UP-FRONT TAXES" FOR PREVIOUSLY EXEMPT OFF-ROAD DIESEL FUEL USE IS ANOTHER AMONG MANY RULES AND PROPOSALS WHICH WILL HAVE A NEGATIVE IMPACT ON OUR INDUSTRY---ESPECIALLY THE DRILLING CONTRACTORS AND VARIOUS WELL SERVICE COMPANIES WHO CONSUME LARGE QUANTITIES OF DIESEL FUEL FOR DRILLING AND DOWN HOLE SERVICE OPERATIONS.

BEFORE I GET INTO SPECIFIC EFFECTS THAT THE NEW TAX RULING WILL HAVE ON MUCH OF THE INDUSTRY, I WANT TO PROVIDE YOU A BRIEF SUMMARY ON THE HEALTH OF THE DOMESTIC PETROLEUM INDUSTRY; MORE ESPECIALLY THAT OF THE PERMIAN BASIN OF WHICH ITS PRIMARY INDUSTRIAL BASE IS THAT OF OIL AND GAS, BUT ALSO, THE DOMESTI INDUSTRY THROUGHOUT MAJOR PRODUCING STATES IN THE NATION, AS WE ALL FACE ..E SIMILAR DIFFICULTIES.

THE CONTRACT DRILLING AND WELL SERVICING INDUSTRY IS IN VERY POOR SHAPE. THE WESTERN COMPANY, ONE OF OUR LARGEST WELL SERVICING COMPANIES, JUST RECENTLY FILED FOR CHAPTER ELEVEN BANKRUPTCY. SEVERAL OF OUR DRILLING CONTRACTORS SUCH AS MGF AND LOFFLAND BROTHERS, HAVE BEEN UNDER CHAPTER ELEVEN PROCEDURES AND CONSTRAINTS FOR MANY MONTHS AND TODAY, ARE STILL STRUGGLING FOR SURVIVAL. WITHIN THE PERMIAN BASIN, NEARLY 40 PERCENT OF OUR FIRMS ENGAGED IN DRILLING AND WELL SERVICES JUST A FEW YEARS AGO, ARE NOW OUT OF BUSINESS. THEIR PLIGHT IS SHOWN MOST DRAMATICALLY BY THE BASIN'S DAILY OPERATING RIG COUNT WHICH WENT FROM A HIGH OF 529 IN JANUARY 1982 TO A LOW OF 74 IN SEPTEMBER 1986. IT IS NOW FAIRLY CONSTANT AT 145 OPERATING RIGS PER DAY.

IN MIDLAND, OUR SECOND LARGEST EMPLOYER OF EMPLOYEES CONTINUES TO BE THE FDIC WHICH QUARTERLY, HOLDS THE NATION'S LARGEST GARAGE SALE, AND WHERE AUCTION SALES REVENUE COME FROM GOODS AND EQUIPMENT OBTAINED FROM FORECLOSURES AND FAILURES OF PETROLEUM INDUSTRY BUSINESSES.

BANK FAILURES HAVE HIT AN ALL TIME HIGH IN TEXAS AND MOST PRODUCING STATES, AS HAVE BUSINESS FAILURES. IN SHORT, WE NEED SOUND LEGISLATION TO ENHANCE OUR INDUSTRY; NOT ADDITIONAL TAX BURDENS WHICH WILL INCREASE OUT GOING CASH FLOW WITHOUT REVENUE GENERATION IN RETURN AND ADD EXTRA OPERATIONAL COSTS FOR GOVERNMENTAL COMPLIANCE PAPERWORK.

WE BELIEVE THE COMMITTEE WOULD LIKE SOME 1987 STATISTICS THAT IT COULD WORK WITH SOME REAL TIME FACTUAL DATA WHICH IS USED IN FORECASTING THE ADVERSE EFFECTS OF THE NEW PRE TAX REQUIREMENTS ON OFF-ROAD DIESEL FUEL PURCHASES.

WE HAVE OBTAINED OUR DATA FROM TWO SMALL INDEPENDENT DRILLING CONTRACTORS, NAMELY GENE SLEDGE DRILLING AND PETERSON DRILLING OF MIDLAND, TEXAS AND TWO OF OUR LARGEST SERVICE COMPANIES, THE WESTERN COMPANY, WHICH RECENTLY FILED CHAPTER ELEVEN FOR REORGANIZATION AND HALLIBURTON SERVICES, WHO FOR THE FIRST TIME IN SEVERAL YEARS, REFLECTED A 1987 PROFIT IN SALES AND SERVICES NATION WIDE.

I REQUEST THE COMMITTEE REFER TO EXHIBIT "A" OF THIS TESTIMONY.

AS PER EXHIBIT "A" BOTH DRILLING COMPANIES DESCRIBED ARE RELATIVELY SMALL, HAVING ONLY FOUR TO FIVE RIGS IN INVENTORY WITH A UTILIZATION RATE OF APPROXIMATELY 75% TO 80% OF TOTAL CAPACITY. AS YOU WILL NOTE, EACH DRILLING COMPANY CONSUMED IN EXCESS OF 650,000 THOUSAND GALLONS OF DIESEL FUEL WITH AN AVERAGE RIG DAILY CONSUMPTION RATE OF OVER 500 GALLONS. CONSIDERING ACTUAL 1987 DATA, IF AN EXCISE TAX OF 15.1 CENTS PER GALLON WAS LEVIED ON GENE SLEDGE DRILLING FOR 1987, THE COMPANY'S TOTAL ADDITIONAL CASH-FLOW OUTLAY WOULD HAVE BEEN $107,000 OR $21,400 PER RIG ANNUALLY. IF YOU ASSUME THAT EACH GENE SLEDGE RIG WAS OPERATING FULL TIME, A SITUATION WE CERTAINLY HOPE TO RECAPTURE, THE COMPANY'S ADDITIONAL CASH OUTLAY DUE TO THE IMPOSITION OF THE EXCISE TAX ON DIESEL FUEL WOULD BE APPROXIMATELY $142,000 PER YEAR.

IN THE CASE OF OUR SERVICE COMPANIES, EXHIBIT "A" DEPICTS FIGURES ON A NATIONAL BASIS.

IT IS UNDERSTANDABLE BY THESE EXHIBITS THAT THE ADDITIONAL CASH FLOW BURDEN COULD BE DEVASTATING, ESPECIALLY TO THOSE SMALL INDEPENDENTS OR COMPANIES FACED WITH CHAPTER 11 PROCEEDINGS OR WHO HAVE OPERATED NEAR OR IN THE RED FOR 1987. FROM ALL KNOWN ESTIMATES FROM ECONOMISTS AND OTHER EXPERTS SUCH AS THE AMERICAN PETROLEUM INSTITUTE, PETROLEUM INFORMATION AND WORLD OIL AND THE OIL AND GAS JOURNAL MAGAZINES, THE DRILLING OUT LOOK AND WELL SERVICING PROJECTIONS FOR 1988 WILL BE MUCH LIKE THAT OF 1987 AND THE INDUSTRY WILL CONTINUE TO STRUGGLE FOR PROFITS. THE ADDITION OF THE EXCISE TAX ON EXEMPT FUELS AND THE CORRESPONDING COSTS FOR COMPLIANCE MAY ONLY HASTEN THE INEVITABLE--THAT OF FURTHER BUSINESS CRISIS OR TOTAL FAILURE.

THE WESTERN COMPANY IS CURRENTLY OPERATING UNDER BANKRUPTCY REORGANIZATION PROCEDURES AND NOT ONLY HAS NOT PROGRAMMED OR BUDGETED FOR THE ADDITIONAL ANNUAL CASH FLOW OF OVER 340 THOUSAND DOLLARS TO MEET EXCISE TAX REQUIREMENTS, BUT CAN ILL AFFORD THE ADDED EXPENSE BURDEN WHEN THEIR REORGANIZATIONAL PROGRAM AS OVERSEEN BY THE COURTS AND IS ONE OF AUSTERE CUTS AND REDUCTIONS IN SUPPORT OF ITS RECOVERY EFFORTS.

HALLIBURTON SERVICES, A DIVISION OF THE HUGE HALLIBURTON COMPANIES COMPLEX, IS MUCH MORE CAPABLE OF ABSORBING THE INCREASED CASH FLOW REQUIREMENT WITHIN ITS ORGANIZATIONAL STRUCTURE, HOWEVER, IT WAS ONLY UNTIL RECENTLY THAT IT SHOWED AN ANNUAL PROFIT AND AN ADDITIONAL LIABILITY OF OVER 1 MILLION DOLLARS AND THE BURDEN OF ADDED ADMINISTRATIVE COSTS WOULD BE A FURTHER DETRIMENT TO ITS CONTINUED RECOVERY EFFORTS.

THE SMALL INDEPENDENT DRILLING COMPANIES AND OTHERS WHO ARE IN FINANCIAL DIFFICULTIES ARE NOT SURE HOW THEY ARE TO MEET THE NEW TAXING OBLIGATIONS.

REGLARDLESS OF THEIR ABILITY TO RECOVER SUCH TAXES BY FILING FOR REFUNDS FOLLOWING THE YEARS END, THE MONEY HAS NOT BEEN BUDGETED NOR IS THERE A SUFFICIENT RESERVE FUND AVAILABLE TO COVER THE ADDED LIABILITY. TO BORROW THE MONEY FROM A BANKING INSTITUTION, WHICH WOULD BE NEXT TO IMPOSSIBLE FOR MANY, WOULD BE ADDING AN ADDITIONAL CASH FLOW LIABILITY IN INTEREST AND WOULD ONLY DEEPEN THE WOUND ABOUT TO BE INFLICTED. THE REMAINING WAY IS TO CHARGE BACK TO THE CUSTOMER TO RECOVER THE ADDITIONAL COSTS---A PROCEDURE TOTALLY COUNTER PRODUCTIVE AS IT WOULD DESTROY THE SMALL INDEPENDENTS ABILITY TO COMPETE IN A HIGHLY COMPETITIVE MARKET PLACE.

WHILE OFF SHORE DRILLING OPERATIONS ARE FAR DISTANT FROM THE PERMIAN BASIN, THE SAME PROBLEM IS SHARED. ACCORDING TO THE INTERNATIONAL ASSOCIATION OF DRILLING CONTRACTORS, A DRILLING CONTRACTOR HAVING A FLEET OF 20 OFF SHORE DRILLING RIGS WOULD USE APPROXIMATELY 500 THOUSAND GALLONS OF DIESEL FUEL PER MONTH WITH AN ADDITIONAL TAX COST OF OVER $900 THOUSAND PER YEAR.

IN SUMMARY

WE BELIEVE THAT A TAX LEVIED ON THE TAX EXEMPT COMMODITIES SUCH AS DIESEL FUEL, FOR THE IDENTIFIED PURPOSE OF STOPPING THE WIDE-SPREAD EVASION OF DIESEL FUEL TAX PAYMENTS TO THE FEDERAL GOVERNMENT IS UNFAIR, UNJUST AND A DEPRESSANT TO BUSINESS ENHANCEMENT. IT IS AN ACTION WHICH PLACES AN UNDUE BURDEN ON THE MAJORITY TO AID THE IRS IN THE INTERNAL DIFFICULTIES OF THEIR DETECTION AND COLLECTION PROCESS. WHILE WE CANNOT SAY THAT SUCH EVASIONS DO NOT OCCUR IN THE OIL PATCH, IT IS HIGHLY UNLIKELY THAT DIESEL FUEL USED TO OPERATE WELL SITE EQUIPMENT IS BEING USED FOR ON-ROAD PURPOSES, JUST AS IT IS ALSO UNLIKELY THAT DIESEL FUEL OR HEATING OIL USED FOR HOME HEATING IS ALSO BEING USED FOR ON-ROAD MOTORIZED VEHICLES. THERE ARE NUMEROUS SAFE GUARDS TO PREVENT SUCH EVASIONS, FULLY QUALIFYING

(TROLEUM INDUSTRY MOTORIZED OFF-ROAD EQUIPMENT IN A CATEGORY WHICH MOST LIKELY, WILL NOT UTILIZE OFF-ROAD DIESEL FUEL FOR ON-ROAD PURPOSES. I WILL BE MOST HAPPY TO FURTHER DISCUSS THESE SAFE GUARDS FOLLOWING THIS PREPARED TESTIMONY.

LASTLY, WE BELIEVE THAT A PERMANENT FIX TO THE NEW TAX WOULD BE AN OUTRIGHT REPEAL OF THE COLLECTION POINT FOR FEDERAL EXCISE TAXES ON DIESEL FUEL AS REQUIRED BY THE OMNIBUS BUDGET RECONCILIATION ACT OF 1987. KNOWING OF THE DIFFICULTIES OF SUCH A REPEAL, THE NEXT BEST ALTERNATE WOULD BE TO PROVIDE AN AMENDMENT TO THE BILL SUCH AS H.R. 3865 PROPOSES, WHICH WOULD PERMIT TAX FREE SALES OF DIESEL FUEL FOR OFF-ROAD USES OR INFLUENCE THE DEPARTMENT OF THE TREASURY TO EXEMPT THE PETROLEUM INDUSTRY FROM SUCH TAXES AS CURRENTLY EXISTS AND AS WHAT IS THOUGHT TO BE A GRANTED AUTHORITY BY THE CONGRESS.

THANK YOU FOR INVITING ME TO APPEAR BEFORE YOU. I WILL BE HAPPY TO RESPOND TO ANY QUESTIONS YOU HAVE ON THIS MATTER.

EXHIBIT "A"

1987 CLASSIFICATION	PETERSON DRILLING	SLEDGE DRILLING
Number of Drilling Rigs	4	5
Number of Drilling Contracts	65	37
Active Drilling Days (All rigs)	1143	1397
Rig Utilization Rate	80%	75%
Diesel Used (Off-Road)	655,321 Gallons	710,546 Gallons
Average Diesel Daily Consumption	573 Gallons	509 Gallons
Diesel Fuel Costs (Off-Road)	$412,852	$585,259
Added Cash Outlay for Excise Taxes	$ 98,953	$107,292

SERVICE COMPANIES

1987 CLASSIFICATION	THE WESTERN COMPANY	HALLIBURTON SERVICES
Number of Diesel Units	726	UNK
Diesel Used (Off-Road)	2,259,290 Gallons	7,500,000 Gallons
Diesel Costs (Off-Road)	$1,581,503	$5,250,000
Added Cash Outlay for Excise Tax	$ 341,153	$1,132,500

PMAA PETROLEUM MARKETERS ASSOCIATION OF AMERICA

Statement of

Gene Hutter, North Central Regional Vice President

Petroleum Marketers Association of America

Before the

Energy and Agriculture Subcommittee

Committee on Small Business

U.S. House of Representatives

On

Diesel Fuel Excise Tax Collection Process

H.R. 3865

March 3, 1988
Washington, D.C.

1120 VERMONT AVENUE, NW ▪ SUITE 1130 ▪ WASHINGTON, DC 20005 ▪ (202) 331-1198

Introduction

Good morning Mr. Chairman and members of the Subcommittee. I am Gene Hutter, Executive Vice President and General Manager of the Wally Hutter Oil Company of Quincy, Illinois. I am the North Central Regional Vice President of the Petroleum Marketers Association of America (PMAA), based here in Washington, and I am appearing on behalf of PMAA. PMAA commends the subcommittee for its active interest in the federal diesel fuel excise tax issue. Just last November 18, this subcommittee held a hearing on another issue of vital importance to petroleum marketers -- the difficulties our industry is having in obtaining underground storage tank insurance. So the interest of this subcommittee is very much appreciated.

The Wally Hutter Oil Company has been in business in downstate Illinois for over 25 years and serves six counties in Illinois and Missouri. We are a full-line petroleum marketer of gasoline and other petroleum products sold under the Shell, Sun, and Mobil brand names. We also have several convenience stores. Hutter Oil Company employs 27 people and that includes me, Mr. Chairman. So you can see, we are a small business. Of particular importance to the subject of this hearing, Mr. Chairman, Hutter Oil Company has over 1,000 farm accounts which represents over half of our total accounts. We also have approximately 300 heating fuel accounts; they are all rural customers.

The Petroleum Marketers Association of America is a federation of 43 state and regional associations which represent over 10,000 companies throughout the United States. Our 43 member associations are listed on Attachment I. Collectively, PMAA members account for approximately 50 percent of the gasoline, 60 percent of the diesel fuel, and 75 percent of the home heating oil sold in the United States. The majority of marketers sell their products in rural America; however, many marketers also operate in urban and suburban markets. Nearly 90 percent are classified as small business by SBA size standards. PMAA's average member company has 22 employees. A flow chart of the petroleum distribution industry in the U.S. is shown as Attachment II.

Background

Mr. Chairman, PMAA has been working on the federal motor fuel excise tax issue for several years now. Our efforts have been directed at both the collection of the 9.1 cents per gallon federal excise tax on gasoline and the 15.1 cents per gallon federal excise tax on diesel fuel. Congress acted first on the gasoline excise tax issue by dramatically changing the collection procedure effective January 1, 1988. This was done as part of the Tax Reform Act of 1986 (PL 99-514) and is addressed in great detail later in this testimony. Allow me first to focus on the primary topic of this hearing -- the changes in the diesel fuel excise collection procedure.

Diesel Excise Tax Collection Process; Congressional Action Forces Industry Change

As part of the Omnibus Budget Reconciliation Act of 1987 (PL 100-203), Congress changed the collection procedure for the 15.1 cents per gallon federal diesel fuel excise tax. This section of the law is schedule to take affect April 1, 1988. Under Section 10502 of that Act, the diesel fuel excise tax will be collected by the "producer". The term "producer" is defined to include refiners, terminal operators, and wholesale distributors who register, report, and post a bond as required by the Internal Revenue Service (IRS). All current tax exempt purchasers including farmers, drilling contractors, marinas, and

other off-road users must, effective April 1 of this year, begin paying the tax and applying for a refund or credit from the IRS. In addition, all retailers who currently have the right to pay the tax to the IRS must also pay it to their refiner or wholesale distributor. Residential home heating oil is exempt from the tax.

The Department of Treasury has the discretion to exempt other users from payment of the tax including state and local governments, diesel fuel used in trains, taxable fuels used for industrial use other than as a motor fuel, and commercial aviation fuel.

Prior to this change, diesel fuel excise taxes were considered a retail tax. The tax was paid to the government by the retailer or end user. However, Congress, as part of the Tax Reform Act of 1986, enacted a procedure whereby a wholesale distributor and retail dealer could mutually agree to have the wholesale distributor collect and remit the diesel fuel excise taxes.

Diesel Excise Tax Collection Process: IRS Inaction Thwarts Congressional Intent

All of the problems with this new collection procedure are not yet known. Despite the fact that this change is scheduled by law to take effect on April 1, IRS has not, as of March 1, issued any proposed regulations or guidance on how the procedure may work. For example, what will be the registration, reporting, and bonding requirements applicable to wholesale distributors? Will IRS be able to process the thousands of registration certificates to be submitted by wholesale distributors and their customers prior to April 1? If not, what steps will IRS take to minimize the disruption to the marketplace caused by delays in approving registration certificates? How will heating oil sales be differentiated from diesel fuel sales since these products are essentially the same? What requirements will heating oil dealers have to comply with to purchase heating oil tax exempt?

Mr. Chairman, these are important questions that need answers and need answers quickly. Granted, Congress didn't give IRS much time to promulgate regulations for a change signed into law on December 22, 1987, that was to take effect on April 1, 1988. In fact, prior to the December 22 Congressional enactment of the Omnibus Budget Reconciliation Act, PMAA wrote to all members of the Senate Finance and House Ways and Means Committees pleading that Congress make the effective date of the diesel fuel change July 1, 1988, or 90 days after IRS issued final regulations. However, the Congress selected April 1, as the effective date, which was a significant improvement over the January 1, 1988, date originally being contemplated. Based on past experience, PMAA doubts seriously IRS's ability to promulgate intelligible regulations to implement this provision prior to April 1. I would invite the Subcommittee's attention to two recent examples of IRS's failure to issue timely regulations. First, on March 1, just two days ago, IRS released a seven page notice of proposed rulemaking relative to the change mentioned earlier that was incorporated in the Tax Reform Act 1986. That law was signed on October 22, 1986, and it took until March 1, 1988, for IRS to issue "proposed temporary regulations". These proposed regulations are to be effective and applied to sales of diesel fuel for use in diesel-powered highway vehicles made after March 31, 1987, and before April 1, 1988. In other words, it took IRS well over a year to come out with regulations that can now only be effective for one month, March 1988, because Congress has subsequently passed another law which will change the diesel excise tax collection procedure as of April 1, 1988!

As a second example, IRS did not come out with their proposed regulations on the changes in the gasoline excise tax collection procedure until November 18, 1987, more than a year after the Tax Reform Act of 1986 was signed into law. In its November 18 notice, IRS solicited public comments until December 18, and then, in the best example of all, had a public hearing on January 5, 1988, four days after the new procedure was scheduled to take effect. Since then, numerous "notices" have been issued to correct errors and clarify confusing passages of the proposed regulations. However, some errors, such as a section that disallows credits or refunds of the LUST tax to state and local governments and hospitals, still remain uncorrected, even though the end of the first quarter is drawing near. As a result, many marketers' customers are incapable of calculating properly the full amount of the refunds.

Mr. Chairman, the marketers PMAA represents and I believe the vast majority of participants in this industry want to abide by the law. We have tried to be as cooperative as possible with government efforts to reduce excise tax evasion. But how can we really be expected to comply with the law, Mr. Chairman, when we are constantly being barraged with conflicting information and last minute changes in the rules coming out of Washington?

Frankly, Mr. Chairman, I believe that Congress is at least partially to blame when it passes comprehensive legislation that weighs 43 pounds at the very last minute. As you know, the subject of this hearing is one little section in that 43 pounds of paper that the President displayed during his State of the Union Address last January 25. I am sure that there are all kinds of other industries around the country that are facing problems just as crucial to them as the motor fuels excise tax issue is to us.

Diesel Excise Tax Collection Process: PMAA Solution

While we are all awaiting direction from the IRS, there are some obvious problems which would require statutory correction. The most obvious of these problems is the requirement that farmers, marinas, and drilling contractors, and other off-road users must pay the tax directly to the wholesaler distributor or refiner. This creates two tremendous problems. First, it means a tremendous loss of cash flow to the farmer and other off-road users. The American Farm Bureau estimates that American farmers would be paying $420 million per year to their suppliers, who would turn that money over to the IRS which would then either refund the money or provide a credit on the farmers' income tax return. This would be another devastating blow to America's agricultural community.

The second problem relates to suppliers of diesel fuel to the farmer. The supplier is, in most cases, a wholesale distributor. By necessity, these distributors often offer liberal credit terms to their agricultural accounts. In some instances, the fuel bill is not paid until the crop is harvested. Credit terms to farmers of 60 or 90 days are not unusual. This means these small wholesale distributors will have a substantial increase in their accounts receivable, thus damaging significantly their cash flow. It also could mean higher losses to bad debts if farmers are unable to pay their bills.

PMAA's proposed solution to this problem is simple. We support an amendment which would allow off-road users of diesel fuel to continue to buy diesel fuel minus the tax. This would include farmers, fishermen, marinas,

drilling contractors, and others. Adoption of this amendment would be advantageous in that there is no justification to require these users to pay a tax they do not owe and then have IRS refund the money through a cumbersome, bureaucratic procedure.

Fifteen bills have been introduced in the House and Senate between the time the second session convened on January 25 and February 29 which address some aspect of the gasoline and diesel fuel excise tax problem. These bills are summarized as Attachment III.

Gasoline Excise Tax Collection Process: Congressional Action, Resulting Problems, and PMAA Solution

Mr. Chairman, as I mentioned earlier in my statement, PMAA is actively working on the federal gasoline excise tax issue as well as the diesel fuel excise tax issue. With your indulgence, I would like to briefly mention what Congress did in 1986 on the gasoline excise tax, the problems it has created, and PMAA's solution.

In Section 1703 of the Tax Reform Act of 1986 (PL 99-514), Congress changed the collection procedure for the 9.1 cents per gallon federal excise tax on gasoline. Under this procedure, which took effect January 1, 1988, the point of taxation is when gasoline leaves the terminal and is loaded into trucks for further distribution. The seller of the gasoline at that point, usually a terminal operator, refiner or importer, would collect the tax from the purchaser, usually a jobber or chain retailer, and remit it to the Internal Revenue Service on a specified payment schedule. Once the gasoline passes the point of taxation (i.e. loaded from the terminal into trucks) no further tax exempt sales are allowed. Purchasers of gasoline that previously bought on a tax exempt basis would have to pay the tax and apply for a refund.

Prior to enactment of Section 1703, the excise tax collection procedure was based on the first sale of gasoline from a "producer" to a non-producer of gasoline. "Producer" was defined to include not only refiners, terminal operators and importers, but also wholesale distributors and chain retailers. This meant that the taxable event could occur at several points in the gasoline distribution process. For example, the taxable event may not occur until the refiner or independent marketer sold product to a motorist at a station he owned and operated.

There are at least three problems with the new system which need to be addressed by technical corrections to Section 1703. First, the clear intent of Section 1703 is that there be no tax exempt sales downstream and that current tax exempt purchasers apply for a credit or refund of taxes paid. However, Congress inadvertently failed to repeal Section 48.6416 of the Internal Revenue Code, which allows suppliers not to pass on to their state and local government customers the taxes already paid on gasoline, and file for a refund of the tax from the IRS. Unfortunately, under Section 6416, only "taxpayers" are eligible to apply directly to the IRS for the refund. Wholesale distributors/jobbers are no longer considered "taxpayers" and must apply to their refiner-suppliers for a refund of the taxes paid but not collected from the government entity. The use of Section 6416 is voluntary on the part of the refiners, however, and some have indicated a willingness to honor this procedure, but several others have not. This means that many state and local governments served by wholesale distributors probably will be unable to take advantage of the provisions of Section 6416. Moreover, refiners have a built-in competitive advantage over wholesale distributors under Section 6416, in that they can sell to state and local governments tax free and deduct that amount from the taxes remitted

directly to IRS. Jobbers on the other hand, must either wait for a refund from their refiners who have chosen to honor Section 6416, or must charge their exempt customers the tax.

The second problem relates to gasohol. Under Section 1703, purchasers of gasoline and ethanol blended at the same terminal are entitled to the reduced tax rate applicable to gasohol of 3 and 4/9 cents per gallon. However, purchasers who buy gasoline at one terminal and ethanol at another (few terminals sell both gasoline and ethanol) may have to pay the full 9.1 cents per gallon tax and apply for a refund from IRS. Currently, IRS is allowing purchasers of gasoline and ethanol from separate terminals the reduced tax rates. However, there are strong indications from IRS that effective April 1, only those gallons purchased and blended at the same terminal will be eligible for the reduced rate.

The final problem relates to the fact that in the petroleum industry, refiners are both suppliers and competitors of wholesale distributors/jobbers. By allowing the refiner to collect the tax from the jobber means the refiner has the use of the jobber's tax money for as much as two to three weeks before the taxes must be paid to the government. The "float" on these tax dollars clearly give refiners a competitive advantage over jobbers.

PMAA recommends that Congress enact one minor change to Section 1703 of the 1986 Tax Reform Act (PL 99-514). This change would allow purchasers of gasoline at the terminal to remit the federal excise tax directly to IRS, provided that the purchaser (wholesale distributor or chain retailer) is registered as a tax remitter and agrees to comply with any bonding or financial responsibility requirements imposed by the IRS. The point of taxation would remain the same (i.e. as product is loaded into trucks for the first time at the terminal). In addition, there would be no tax exempt sales of gasoline, except those authorized under Section 6416 of the Internal Revenue Code to state and local governments.

There are several advantages to this amendment. First, it would correct the competitive advantage refiners have over marketers by giving marketers the right to remit the tax directly to IRS based on their purchases from the refiner. Secondly, it would allow those state and local governments supplied by wholesale distributors/jobbers to take advantage of Section 6416 and buy gasoline tax exempt. It would also places jobbers and refiners on the same competitive basis in serving state and local accounts. Third, the proposed amendment, by allowing wholesale purchasers at the terminal to remit the tax, would enable gasohol blenders to pay the reduced tax rate to IRS directly on those gallons that are blended. Finally, the change would still provide IRS a clear-cut audit trail to prevent tax evasion. IRS can merely match a wholesale distributor/jobber's purchases at the terminal with the taxes remitted. The only justifiable allowance for not remitting taxes on every gallon purchased would be for sales to state and local governments and the reduced tax rate applicable to gasohol. Moreover, the bonding and reporting requirements would be a significant deterrent to evasion.

This proposed amendment, sponsored by Rep. J. J. Pickle (D-TX), was adopted by the House of Representatives as part of the Omnibus Budget Reconciliation Act on October 29, 1987, but was dropped in conference along with other provisions of that bill which did not increase revenue to the federal government. This was consistent with the White House - Congressional Budget Summit agreement of November 18, 1987.

Conclusions

Mr. Chairman, the Petroleum Marketers Association of America would again like to commend you for holding this hearing. I am just one small businessman, an independent petroleum marketer, living and working in Quincy, Illinois. I never doubted it before, Mr. Chairman, but these last few years have sure brought home to this small businessman the fact that what you Congressman and Senators do here in Washington, as well as the people in all those agency buildings downtown, can sure have a profound effect on my life. You know, especially when you own and operate a small business like I do, you don't just get up in the morning, go to work, punch in, do what is required, punch out, go home and forget all about it. I have to constantly think about and deal with the laws and regulations that come out of Washington, not to mention my own state capitol of Springfield. Superfund, EPA, IRS, OSHA, Clean Air Act requirements, Labor Department regulations, etc., etc., etc., may all just be abstract terms to you, but I can tell you that figuring out all those things and trying to comply with them take up a large part of my life.

In conclusion, I would hope that Congress would do what it can to encourage IRS to get its act together quickly. Secondly, PMAA urges that Congress approach the gasoline and diesel fuel excise tax issues comprehensively along the lines of the proposals outlined earlier in my statement as soon as possible. This hearing and the just-announced March 18 Senate Finance Energy and Agricultural Taxation Subcommittee hearing on this subject are certainly encouraging developments.

Thank you Mr. Chairman and members of the subcommittee. I will be happy to try to respond to any questions you may have.

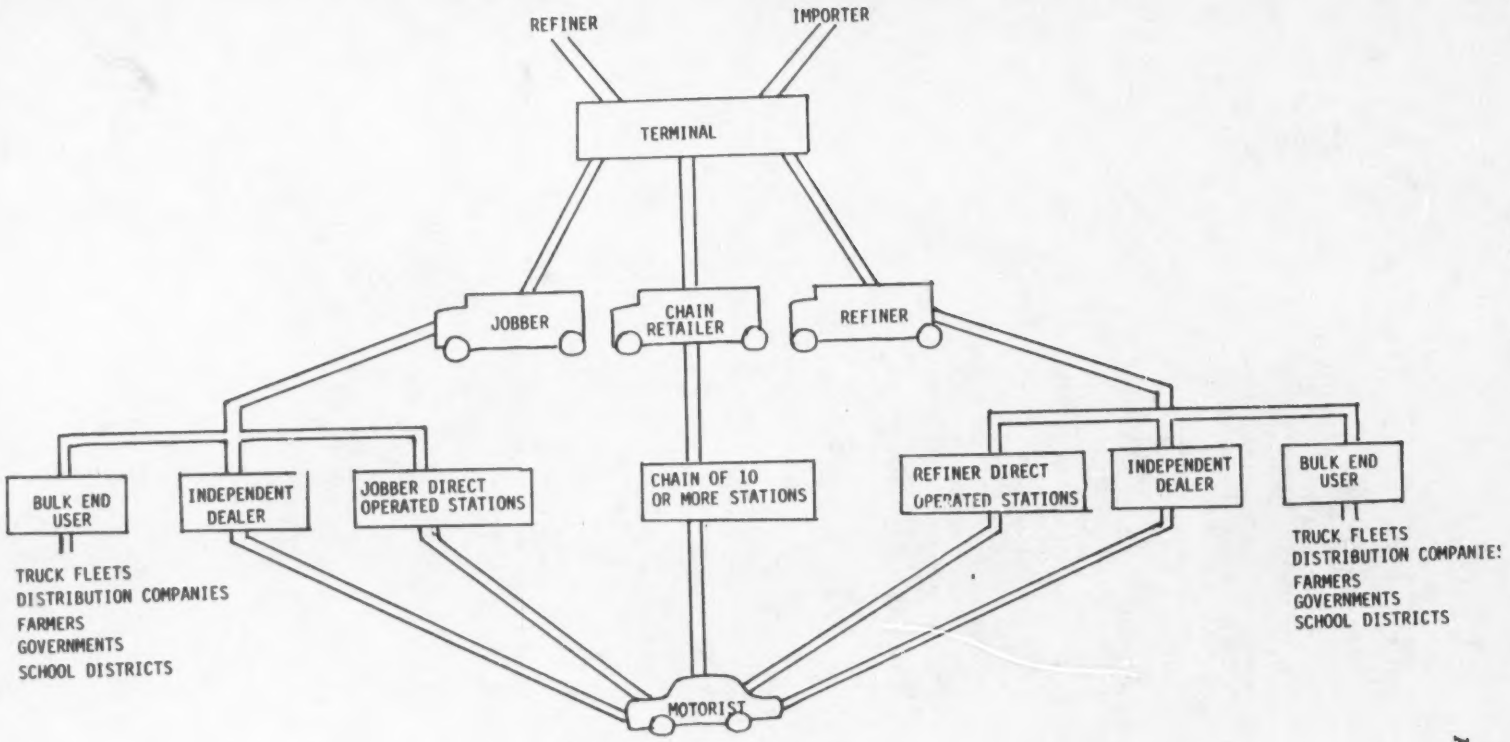
ATTACHMENT I

MEMBERS OF THE PETROLEUM MARKETERS ASSOCIATION OF AMERICA

The Petroleum Marketers Association represents the independent petroleum marketers who are members of these state and regional trade associations:

Alabama Oilmen's Association
Arizona Petroleum Marketers Association
Arkansas Oil Marketers Association, Inc.
California Independent Oil Marketers Association
Colorado Petroleum Marketers Association
Independent Connecticut Petroleum Association
Florida Petroleum Marketers Association
Georgia Oilmen's Association
Idaho Oil Marketers Association
Illinois Petroleum Marketers Association
Indiana Oil Marketers Association, Inc.
Petroleum Marketers of Iowa
Kansas Oil Marketers Association
Kentucky Petroleum Marketers Association
Louisiana Oil Marketers Association
Maine Oil Dealers Association
Michigan Petroleum Association
Mid-Atlantic Petroleum Distributors Association, Inc.
Mississippi Petroleum Marketers Association
Missouri Oil Jobbers Association
Montana Petroleum Marketers Association
Nebraska Petroleum Marketers, Inc.
Nevada Petroleum Marketers Association
Independent Oilmen's Association of New England
Fuel Merchants Association of New Jersey
New Mexico Petroleum Marketers Association
Empire State Petroleum Association
North Carolina Petroleum Marketers Association
Northwest Petroleum Association
Ohio Petroleum Marketers Association
Oklahoma Oil Marketers Association
Oregon Petroleum Marketers Association
Pennsylvania Petroleum Association, Inc.
South Carolina Oil Jobbers Association
South Dakota Petroleum Marketers Association
Tennessee Oil Marketers Association
Texas Oil Marketers Association
Virginia Petroleum Jobbers Association
Washington Oil Marketers Association
Western Petroleum Marketers Association
West Virginia Petroleum Marketers Association
Oil Jobbers of Wisconsin, Inc.
Wyoming Petroleum Marketers Association

The Petroleum Marketers Association of America is located at 1120 Vermont Avenue, N.W., Suite 1130, Washington, D.C. 20005. Telephone (202) 331-1198.



PMAA: 8/87

ATTACHMENT II

PMAA PETROLEUM MARKETERS ASSOCIATION OF AMERICA

ATTACHMENT III

GASOLINE/DIESEL FEDERAL EXCISE TAX COLLECTION PROCEDURE
Legislation introduced January 25 through February 29, 1988.

BILL	SPONSOR	COSPONSORS THRU 2/29/88	DATE OF INTRO	COM.	NOTES
		HOUSE			
H.R. 3844	Daub	Dorgan (orig.) 58 total	1/25/88	W&M	Farm Diesel, Gasoline, Gasohol.
H.R. 3850	Jontz	20 orig. 57 total	1/25/88	W&M	Farm Diesel.
H.R. 3865	Combest	23 orig. 69 total	1/27/88	W&M	Farm/Off-highway Diesel.
H.R. 3866	de le Garza	11	1/27/88	W&M	Farm/Off-highway Diesel.
H.R. 3881	Ms. Smith/NE	19	1/28/88	W&M	Farm Diesel.
H.R. 3892	Neal	37	2/02/88	W&M	State & Local Gov't. Gasoline.
H.R. 3985	Whitten	0	2/22/88	W&M	Farm Diesel, Gasoline, & Gasohol.
H.R. 3989	Inhofe	0	2/24/88	W&M	Farm/Drilling Diesel, State & Local Gov't. Gasoline.
H.R. 3990	Alexander	0	2/24/88	W&M	Farm/State & Local Gov't Diesel, Gasoline.
H.R. 4000	Horton	0	2/24/88	W&M	State & Local Gov't. Diesel.
H.R. 4007	Schuette	2	2/24/88	W&M	Farm Diesel, Farm Gasoline.
		SENATE			
S. 2003	Gramm	24	1/25/88	Fin.	Farm Diesel.
S. 2062	Nickles	4	2/17/88	Fin.	State & Local Gov't. Gasoline.
S. 2067	Conrad	1 orig. 2 total	2/17/88	Fin.	Farm Diesel, Gasoline, Gasohol.
S. 2075	Daschle	12	2/19/88	Fin.	Farm Diesel.

gr: 3/1/88

STATEMENT OF AMERICAN PULPWOOD ASSOCIATION

VICE PRESIDENT RICHARD LEWIS

ON THE

IRS TAXATION OF DIESEL FUEL FOR OFF-ROAD USE

BEFORE THE

SUBCOMMITTEE ON ENERGY AND AGRICULTURE

COMMITTEE ON SMALL BUSINESS

MARCH 3, 1988

The American Pulpwood Association appreciates the opportunity to provide oral and written comments on the issue of tax-free sales of diesel fuel for off-road use.

Before I start, let me mention that the American Pulpwood Association Inc. is a nationwide, non-profit trade association responsible for issues that surround the safe and efficient harvest and transportation of forest products from the woods to the mill. APA members include the small businessmen independent logging contractors who harvest and transport pulpwood and timber, firms which purchase pulpwood and manage forest lands, and equipment companies that manufacture pulpwood and timber harvesting and processing equipment.

Like our colleagues in the farm community, we ask you to support and cosponsor legislation that will permit independent logging contractors to continue to buy tax-free diesel fuel that is used for off-highway felling, skidding, and loading operations which are performed to move timber and pulpwood from the forest to a point where it can be put on a truck. Like many other off-highway fuel users, our members were caught by surprise by the provisions of the 1987 Budget Reconciliation Act, which changed the diesel fuel tax collection point from the retail to the wholesale level.

This off-road diesel fuel tax collection will have a significant undesirable impact on our nation's independent logging contractors. On a nationwide basis, these logging contractors use feller-bunchers, delimbers, forwarders, loaders, cable yarders and a variety of other diesel-powered off-road equipment to harvest some 227 million cords (or cord equivalents) of pulpwood and saw timber each year. We know from past studies that it takes an average of two gallons of diesel fuel per cord to harvest these trees, move them to roadside, and load them on road trucks. This means that these contractors are using approximately 454 million gallons of off-road diesel fuel each year. If the IRS starts collecting a 15¢ per gallon tax on this off-road fuel on April 1, the nation's logging contractors will end up coughing up approximately 68-million dollars each year, and then having to file for a refund or tax credit to get their money back.

The impact of the collection of off-road diesel fuel taxes on individual logging contractors is significant. We gathered some data (see attached) that indicates that these small businessmen will have negative cash flow impacts of $1,000 to $33,000 due to the proposed collection of tax on off-road diesel fuel.

During my frequent visits to logging operations across the nation, I've noted that independent logging contractors are small-businessmen who operate on very tight profit margins. They work hard to make ends meet and they have the same type of cash flow problems that many small, independent businesses experience. Requiring these logging contractors to pay up front tax money on off-road use of diesel fuel is unfair and will cause severe economic problems for some whose businesses already are in fragile financial condition. On behalf of these independent logging contractors, let me say that what IRS is proposing, collecting tax money and then refunding it to them sometime in the future, amounts to what we think is an interest-free loan and an unconscionable practice.

Although we are not fully up to speed on the proposed IRS refund system, we know that the many small logging contractors who use less than 7,000 gallons of off-road fuel quarterly will be hit the hardest. These off-road diesel tax dollars will probably take as long as 14 months to find their way back to independent logging contractor business accounts. We're also concerned that some independent logging contractor operations may not have taxable income in a given year against which an off-road diesel fuel tax credit could be applied. In this case, we assume the credit would be carried forward and again, feel this is unfair because independent logging contractors may need this money to help with cash flow problems.

We're in complete support and will work for passage of the Combest bill (HR 3865) and the de le Garza bill (HR 3866), which both permit tax-free sales of diesel fuel used off-road. We'll also be working to encourage Congressman Daub, Congressman Smith, Congressman Jontz, and Senator Gramm to change the wording in their bills (which currently only cover farm operations) to include other aspects of agriculture and forestry including the planting, growing, cultivation, protection, and logging of timber and pulpwood.

We've not had the time or means to quantify the impact of this off-road diesel fuel tax collection on our members who own and manage forest land. We conservatively estimate mechanical site preparation, reforestation, road building and forest management operations on their 69-million acres of industrial forest holdings use 100-million gallons of diesel fuel per year .... which accounts for another 15-million-dollar cash flow impact on these companies. This does not include the off-road diesel fuel use on small forest holdings, which account for about 70% of the nation's commercial forest land.

To those IRS and other administration tax executives who are here, we respectfully ask for an agriculture and forestry "deferment" or "exemption" from this off-road diesel fuel tax collection at the wholesale level until we can achieve the passage of legislation which will permit tax-free sales of diesel fuel for off-road use.

We thank you for calling this hearing on an issue of great importance to our independent logging contractor members. We hope that you and your colleagues will be able to quickly pass some legislation which will correct the unfair taxation of off-road diesel fuel that is used in agriculture and forestry.

EXAMPLES OF INDIVIDUAL LOGGING CONTRACTOR IMPACTS FROM EXCISE TAX COLLECTION ON OFF-ROAD DIESEL FUEL USED FOR TIMBER AND PULPWOOD HARVESTING

SMALL LOGGING CONTRACTORS

1. Bucky Williams, Wilcox, PA

Crew size:	Two 2-man crews.
Equipment:	Two skidders. One cable yarder
Off-road diesel fuel consumption:	Approx. 7,000 gal./year
Cash flow impact:	-$1,050.00

2. Ray Hunt, Omega, GA

Crew size:	One crew.
Equipment:	One feller-buncher. One grapple skidder. One loader.
Off-road diesel fuel consumption:	22,500 gal./year
Cash flow impact:	-$3,375.00

3. H. C. Salter, Alexandria, LA

Crew size:	One crew.
Equipment:	Two skidders. One feller buncher. One loader.
Off-road diesel fuel consumption:	15,330 gal./year
Cash flow impact:	-$3,300.00

Additional note: Mr. Salter states his diesel fuel supplier is preparing to retroactively collect .15/gal. excise tax back to April 1, 1987!

LARGE LOGGING CONTRACTORS

1. Earl St. John, Spalding, MI

Crew size:	Seven crews averaging 5 men each.
Equipment:	Mix of skidders, feller-bunchers, slashers, bulldozers, graders, delimbers, etc.
Off-road diesel fuel consumption:	218,000 gal./year
Cash flow impact:	-$32,700.00

2. Bennett Timber Co., DeRidder, LA

Crew size:	Twelve 2-man crews.
Equipment:	One prehauler per crew (total 12)
Off-road diesel fuel consumption:	27,300 gal./year
Cash flow impact:	-$4,095.00

3.	Deck Trevitt Logging, Forsyth, GA	
	Crew size:	Two 5-man crews
	Equipment:	Two feller-bunchers Three grapple skidders Two Hydraulic loaders One crawler tractor One motor grader
	Off-road diesel fuel consumption:	57,000 gal./year
	Cash flow impact:	-$8,550.00
4.	Pine Timber Co., Oglethorpe, GA	
	Crew size:	Two 6-man crews.
	Equipment:	Four grapple skidders. Two feller-bunchers. Four hydraulic loaders. Two crawler tractors. One motor grader.
	Off-road fiesel fuel consumption:	65,000 gal./year
	Cash flow impact:	-$9,750.00

PRESENTED BY HOWARD MENAKER

TESTIMONY

OF THE

NATIONAL ASSOCIATION OF TRUCK STOP OPERATORS

TO THE

SUBCOMMITTEE ON ENERGY AND AGRICULTURE

OF THE

UNITED STATES HOUSE OF REPRESENTATIVES

COMMITTEE ON SMALL BUSINESS

DIESEL FUEL EXCISE TAX COLLECTION PROCESS

03 MARCH 1988

I am Howard Menaker and I appear here today on behalf of the National Association of Truck Stop Operators, ("NATSO") the national trade association of the truck stop industry.

NATSO represents over 1000 full service stop truck stops who provide most of the highway food, fuel, lodging and repair on interstate and major highways across the nation. Most importantly, as pertains to these hearings today, some two-thirds of all diesel fuel sold in the United States is sold through truck stops. This fuel is used for both on-road and off-road vehicles.

NATSO strongly supports the concept of restoring the exemption from federal excise tax on diesel fuel to farmers and other off-road users. There has never been an intention to tax this use in the same way as the use of diesel fuel by on the road vehicles. The provisions on diesel fuel contained in the Budget Reconciliation Act of 1987 were reactions to problems that, indeed, did exist -- problems of non-reporting or incorrect reporting of diesel taxes. These problems were real and NATSO on many occasions offered its assistance and its

advice to the Internal Revenue Service regarding methods to improve the collection of appropriate diesel taxes. It was with good intentions to improve collection that the provisions were included in the Budget Reconciliation Act, but as sometimes happens, good intentions resulted in the problems that you have heard detailed here today. We are faced with a burdensome credit and refund system which allows the federal government to use money that the farmer and other small businesses need for their very survival, and which they do not owe to the IRS.

NATSO shares the common goals of seeing that the maximum amount of taxes are collected and helping our small businesses, but we warn that good intentions could again result in unintended problems for small businesses if we are not extremely careful. If the exemption for farmers and other off-road users of diesel fuel is restored without moving the point of collection of that tax back to the retail sale, we will only have shifted the burden and created a new set of problems. There is no way to accurately determine the final use of diesel product at any point in the production or distribution chain, except at the point of final sale. If the taxable status (that is, tax free or taxable) nature of that product is to be determined by the ultimate use, then that determination and the collection of the tax based on that

determination must occur at the retail sale, not when the retailer purchases from the wholesaler distributor.

If the exemption is restored without moving the point of collection back to the retail purchase, we face two alternatives and neither is very desirable. If the tax is not paid by the farmer because it is a tax exempt sale, and yet the retailer must pay that tax at the time of purchase to the wholesale distributor, then we have merely shifted the problem. The retailer now is in double jeopardy. He does not collect the tax but he has to pay it. And who suffers? That retailer, the smallest business person in the distribution chain pays a tax that he does not owe. Any credit or refund proposal which might be suggested by the IRS only recreates the problem we are trying to solve for the farmer today. Will we have accomplished anything?

If on the other hand, we try to avoid that problem by allowing the retailer to attempt some apportionment of on-road versus off-road use at the time of wholesale sale, then we are once again inviting incorrect reporting, or worse yet, evasion by some less honest individuals who would buy fuel claimed for off-road use, and later pump it into trucks for on-road use. As mentioned before, there is simply no way to make the

determination of ultimate use at the time of purchase from the wholesale distributor. The whole attempt of budget reconciliation last year was, and our goal today must be, better enforcement and not bigger loopholes, more problems, or shifting unfair tax burdens.

This leads us to the conclusion that if this Committee recommends that the off-road exemption for farm and other uses of diesel be restored, and it should be, then the collection of the tax at the retail level must be restored with it. There is simply no other way.

Part of the reason for the problems we face today is that the changes of last year were not carefully thought through. There are only twenty-eight days to the implementation date for those changes. Let us not try to rush through this issue without considering all the effects on farmers and other small businesses, and risk more damage. We urge this committee to press the full Congress for delay in the implementation date to allow time for careful consideration of the alternatives, so that we do not make another set of mistakes. NATSO proposes that January 1, 1989 should be the new date of implementation of the changes made in 1987.

More importantly, in solving the problems brought about in the 1987 tax legislation let us not cause others of equally dire consequences to small businesses. Let us not simply shift the burden onto someone else's back. NATSO is ready to discuss at any time with you, the sponsors of the current bills, or your staff, solutions to these problems. There are solutions which would help decrease the tax evasion and incorrect reporting and increase the rate of collection of taxes but which would perserve the rights and economic viability of small businesses. Thank you very much, Mr. Chairman, and I will be happy to answer any questions.

Testimony of

Mr. Frank Willis

of

The Associated General Contractors of America

Presented to the

Committee on Small Business

Subcommittee on Energy and Agriculture

United States House of Representation

March 3, 1988

on the Topic of

Repeal of the Up-Front Diesel Fuels

Tax Exemption for Off-Highway Business Use

AGC is:

* More than 32,500 firms including 8,000 of America's leading general contracting firms responsible for the employment of 3,500,000-plus employees;

* 104 chapters nationwide;

* More than 80% of America's contract construction of commercial buildings, highways, industrial and municipal-utility facilities.

87-359 O - 88 - 4

Mr. Chairman and Members of the Committee, my name is Frank Willis. I am President of Willis Construction Company, a highway construction firm in Florence, South Carolina. I am also a member and National Director of the Associated General Contractors of America, a national trade association representing over 32,000 of this nation's leading general contracting construction firms and affiliated businesses.

I am accompanied here today by David Lukens, Director of AGC's Highway Division. I am pleased to appear before you today to discuss the adverse effects on the construction industry of the repeal of the up-front diesel fuels excise tax exemption. AGC most appreciates the Committee's willingness to examine this issue and appreciates the opportunity to present our views to the Committee.

Mr. Chairman, as an industry comprised primarily of small businesses, the repeal of the up-front diesel fuels tax exemption comes as a special hardship to construction. Construction is an energy intensive industry, consuming large quantities of diesel fuel in off-highway uses, such as earth moving for highway and dam projects and fueling asphalt hot-mix plants and paving machinery.

Since the diesel fuels tax is a user-fee, assessed on highway users to pay their share of the construction and

rehabilitation costs of the nation's highway system, off-highway uses have rightfully been exempt from the tax in the past.

The repeal of the up-front exemption may at first seem like a small change in tax law; however, the change brings major cash management problems to the construction industry.

To give the Committee some insight into the problem from the construction industry's standpoint, I will highlight a number of aspects of this change that are particularly troubling to our industry.

First, it is important to consider the quantity of diesel fuel that even a typical small contractor uses in off-highway construction activities over the course of a year. AGC conducted a survey in December to determine the impact of the tax change. The survey indicated that small highway contractors, on the average, use 200,000 - 300,000 gallons of diesel fuel in off-highway activities each year; small to medium sized asphalt paving contractors use 600,000 - 700,000 gallons of diesel fuel annually; and one of AGC's larger contractors, who constructs major dams, uses up to 8 million gallons of diesel fuel in one year.

At 15.1 cents per gallon, the cash flow implications of this tax change are obviously very significant to these contractors. For that average highway contractor using 200,000 to 300,000

gallons of diesel fuel each year, the firm will carry an additional $30,000 - $45,000 annual cash flow burden; the asphalt paving contractor will carry an additional $90,000 - $105,000 cash flow burden, and the large contractor will carry an additional $1.2 million annual cash flow burden. For small, medium, and large contractors, these are all sizeable sums of cash that the contractors will now have to pay the government up-front.

Second, we understand that the Treasury is contemplating a quarterly refund process for refunds of $1,000 or greater, and an annual process for other refunds. Anticipating that there will be a flood of refund applications, we expect that there will be a delay, and likely, a lengthy delay in processing refund checks -- All without interest for the government's use of our money.

Third, construction contracts are often long term in nature and fixed price. Since this tax change will significantly increase the price of fuels on existing contracts, the construction industry will have to absorb these increases within already agreed upon contract prices.

AGC recognizes and fully supports the desire of Congress to close loopholes in the tax system which permit the unscrupulous to evade payment of taxes they rightfully owe. We have a hard time understanding, however, the fairness of a tax provision

which requires individuals to pay tax for a legitimate non-taxable activity and then apply for a refund which they hopefully will receive sometime in the future, without interest. Combined with all the other tax accounting changes that have taken place over the past two years which have adversely affected the construction industry, we have to say -- Enough is Enough!

Since enactment of the exemption repeal provision in December of last year, construction, agriculture, and other industries have been seeking a remedy to the situation. In response, a number of bills have been introduced addressing different industries' concerns. In the House, H.R. 3685 sponsored by Congressman Combest and 75 co-sponsors, restores the exemption for agriculture and most other off-highway uses. In terms of equity, this is the fairest approach.

As you are undoubtedly aware, four categories of diesel fuel users were specifically mentioned in the exemption repeal provision passed last December as deserving of consideration for continuation of the up-front exemption -- diesel trains, non-commercial aviation, non-motor industrial uses and state and local governments.

The Treasury is authorized to screen entities in these four categories, on a case-by-case basis, and convey tax exempt status to them provided they meet certain requirements documenting their non-taxable use. We understand that, provided the IRS has

sufficient manpower to screen and audit entities which apply for the up-front exemption, the revenue impacts of this process should be negligible.

AGC believes that if this process is fair for these four categories of diesel fuel users, the process should be extended to other qualified off-highway business use. We fail to see the equity in limiting the opportunity to seek the exemption to some types of industries and users, while excluding others with an equal claim to the exemption.

As an industry, construction will stand toe to toe with agriculture, aviation and any other qualified off-highway user of diesel fuel. Upon examination, AGC believes the Committee will fail to distinguish any reasonable difference in the legitimacy of construction's non-taxable status compared with the other qualified off-highway uses.

In closing, Mr. Chairman, AGC urges the Congress to quickly address the inequity of the repeal of the diesel fuel tax exemption for all industries which have legitimate non-taxable uses. The April 1 effective date is almost upon us.

Again, AGC most appreciates this Committee's desire to examine the issue. We look forward to working with this Committee as you examine options to address the problem.

STATEMENT OF ROBERT L. NASH
PRESIDENT, GEORGIA FARM BUREAU FEDERATION
BEFORE THE HOUSE SMALL BUSINESS SUBCOMMITTEE ON ENERGY AND AGRICULTURE
DIESEL FUEL EXCISE TAX COLLECTION PROCESS
H.R. 3865
March 3, 1988

Mr. Chairman and members of the Subcommittee, thank you for the opportunity to speak on behalf of over 170,000 Georgia Farm Bureau members. The provision in the Omnibus Budget Reconciliation Act of 1987 which changes the collection point for diesel fuel tax from the retail to the wholesale level will create a very serious problem for Georgia farmers and those in agriculture throughout the nation. We question the intent of Congress to raise revenue in the current fiscal year and refund it the next year as an unfair practice. We feel that there is no justification for this change when farmers are trying to recover from low income years and low market prices.

It is possible that the intent of this legislation was to prevent violation of the off-road purchase of fuel used in on-road vehicles. However, there are presently state and federal laws which control the use of off-road purchases of fuel and this area is well regulated and monitored with monthly and quarterly reporting and payment of fuel taxes. We feel that there is no justification for enacting this legislation with the intent of finding violators.

The fact that Congress continues to exempt off-road use from the excise tax provides further proof that the intent of this legislation was merely to provide a vehicle to collect revenue for budget-balancing purposes. However, the statute provides the Secretary of the Treasury

with the authority to exempt certain uses such as diesel powered trains, commercial aviation, and state and local governments. We feel that agriculture, as a large user of diesel fuel, deserves the same discretionary exemption.

This new burdensome law would cause cash flow problems for our farmers and would also result in higher interest costs. The latest available statistics show that in 1982, Georgia farmers used approximately 62,162,162 gallons of diesel fuel. Using this same estimated figure for 1987 and multiplying by the 15.1 cents/gallon which farmers will pay as a result of the new legislation, results in a total of $9,386,486.40 in capital outlay which the government would be holding from Georgia farmers alone. When a 12% interest rate is considered, because of the need for farmers to secure additional operating loans, this legislation could cost Georgia farmers an additional $1,126,378 in interest. Because farmers are exempt from the diesel fuel tax for off-highway use, it seems illogical to force them to pay the tax and then file for a refund or tax credit.

Agriculture is a high user of short-term production credit. Many farmers secure their loans from governmental or quasi-governmental agencies such as the Farmers Home Administration or the Farm Credit System. With this new legislation, the federal government would not only be provided with interest free loans from farmers but would also force farmers to pay additional interest to the government on operating loans borrowed through these agencies.

Most farmers in Georgia probably would not qualify for the quarterly refund requirement of $1,000 or more and would be required to wait until the end of the tax year to file for a refund or tax credit.

Many farmers may not have a taxable income against which a credit could be applied.

Mr. Chairman and members of the Subcommittee, Georgia farmers are beginning to see a slight upturn in the agricultural economy in our state. However, we are in no position to provide interest-free financing to the federal government, especially on a tax that we do not owe. At this critical time, Georgia farmers need every available penny to continue rebounding from the agricultural crisis that has been upon us in the past years. We find it ironic that the federal government has developed seminars to educate small businessmen and farmers in methods of reducing debt obligation and then essentially generate more debt obligation by the enactment of this burdensome new law.

Farm Bureau has long been an advocate of less government spending. In addition to the added costs to farmers from bookkeeping and higher interest costs, the government itself will incur more expenses because of the refund process. It is impossible to know exactly how much this entire process would cost the American taxpayers.

We believe that it is fitting that the Subcommittee on Energy and Agriculture of the Committee on Small Business is probing this critical issue. Farmers are small and large business people just the same as those on main street. It is important for farmers to be able to meet their debt obligation just as it is important for any other business person. This new law would severely delay the ability of farmers to meet their debt obligation.

As you are aware, several bills have been introduced to eliminate this impending problem. We appreciate the support of many members of

this subcommittee who are sponsors and co-sponsors of pending bills. We especially thank you for holding this hearing today. We trust that the Congress will take action to correct this unjustified legislation before it takes affect on April 1.

Thank you.

GEORGIA
OILMEN'S
ASSOCIATION
GOA
404-938-0775
3581 Habersham at Northlake
Tucker, Georgia 30084

February 25, 1988

The Honorable Charles F. Hatcher
Chairman
House Small Business Subcommittee
for Energy and Agriculture
405 Cannon Building
Washington, D. C. 20515

Dear Mr. Chairman:

I am Richard Grist from Blakely, Georgia, and I am in the business of petroleum marketing and farming. Today, I am representing the Georgia Oilmen's Association, an organization composed of three hundred and forty (340) small businesses that market gasoline, diesel fuel, oils, and other petroleum products. I hope to be able to illustrate to your committee the drastic impact that the Budget Reconciliation package, passed by Congress, will have on the small petroleum dealer, especially one operating in an area that is primarily supported by agriculture and forestry.

The portion of this law that is most disturbing to those of us who market petroleum, is the one that requires us to charge the fifteen and one tenth cents per gallon federal excise tax to consumers using the fuel for off-highway purposes. These people do not owe this money, and we feel that it is unjust for them to be required to pay it. This, however, is only the beginning of the problem.

Nearly all agricultural sales of diesel fuel are credit sales. Of the two and one half million gallons that I sell yearly, less than one percent is sold as a cash on delivery transaction. Charging the extra .151 cents per gallon tax will cause my diesel fuel accounts receivable to go up approximately twenty three percent. Also, in an agricultural area one is never able to collect all of his accounts in thirty days. On September 31 of 1987, my accounts receivable totaled $368,877.23. Of this amount, $97,810.00 was over thirty days old. Of that $97,810.00, $36,793.00 was over ninety days old. These figures, I believe, show the problem that already exists. This problem will only be compounded by adding a tax that the oil jobber will have to carry for the farmer, who does not really owe the tax in the first place.

Some might ask why the petroleum marketer should be so upset over tax money that will be refunded the following year. But the truth of the matter is that most small businesses and farmers do not have bookkeeping facilities to capture daily all the data needed to file for a refund. The farmer would then turn to his supplier, and the only way our business would produce these records would be to review each invoice written during the year. Performing this function for

one hundred fifty accounts would be very time consuming as well as very expensive. It seems to me that it would also be a great expense for the IRS to process these claims.

As everyone knows, the agricultural economy is very unhealthy. Each year we have an increase in bankruptcies. One petroleum supplier in South Georgia has lost thirty eight accounts to bankruptcy in the last four years. The losses we sustain from these accounts are hard; if they are increased by twenty-three percent, the situation will be impossible.

Many of our accounts are financed by the Farmer's Home Administration. Of these, some are already three months delinquent on their fuel bills because of last year's poor crops, putting them behind before they get started. But to further complicate their problems, not one loan applicant from our county FHA office has had the .151 cents tax increase figured into his 1988 fuel budget.

Figures supplied by the U. S. Extension Service estimate that from one hundred to one hundred ten million gallons of fuel will be consumed for agricultural and forestry use this year in Georgia. The tax on this fuel will be approximately fifteen million

dollars. This is money that will leave the already poor economy of rural Georgia, and this exodus of revenue will affect each person living there in a negative way.

From this testimony I hope you will see what a devastating effect this law will have on the petroleum marketer and the farmer. Mr. Chairman, members of the committee, we ask you to take immediate action to correct this unjust, inequitable situation facing us.

Yours truly,

Richard Grist

Richard Grist
Georgia Oilmen's Association

RG/pbm

AMERICAN BUS ASSOCIATION

1025 CONNECTICUT AVENUE, N.W., WASHINGTON, D.C. 20036 (202) 293-5890

Norman R. Sherlock
President and
Chief Executive Officer

STATEMENT OF NORMAN R. SHERLOCK

PRESIDENT AND CHIEF EXECUTIVE OFFICER

THE AMERICAN BUS ASSOCIATION

ON

DIESEL FUEL EXCISE TAX COLLECTION PROCESS

BEFORE THE SUBCOMMITTEE ON

ENERGY AND AGRICULTURE

OF

THE SMALL BUSINESS COMMITTEE
U.S. HOUSE OF REPRESENTATIVES
WASHINGTON, D.C.

MARCH 3, 1988

On behalf of the American Bus Association, I appreciate this opportunity to comment on the diesel fuel excise tax collection/exemption process. I commend the Committee for conducting this hearing. The American Bus Association represents more than 3,500 companies involved with bus regular route, tour and charter, airport and commuter services, and in businesses that are related to travel and tourism.

1. Collection Procedures for Diesel Fuel Excise Tax Modified by Omnibus Budget Reconciliation Act of 1987

As you know, the Omnibus Budget Reconciliation Act of 1987 changed the collection point of the diesel fuel excise tax. Previously, the tax could be collected on the sale by the retailer to the ultimate consumer of the fuel; the new law provides that the tax be collected at the wholesale level on the sale of fuel to any taxable fuel retailer. Collection of the excise tax on the sale of diesel fuel by wholesale dealers has has been made mandatory for all sales.

In addition, the new law repealed all exemptions for tax free sales and all provisions permitting exempt sales beyond the wholesale level. However, in the Conference Report, the Treasury Department was given discretionary authority to exempt from the tax certain sales where the purchaser demonstrates that the fuel will be used in a non-taxable use and he registers and posts such bond as Treasury may require. Sales that may be exempted included:

(1) Diesel fuel sold for use as fuel in a diesel powered train,

(2) Aviation fuel sold for use as a fuel in an aircraft in commercial aviation,

(3) Taxable fuel sold for industrial use other than as a motor fuel, and

(4) Taxable fuel sold for the exclusive use of any state, a political subdivision of a state, or the District of Columbia.

All other exemptions from motor fuel excise taxes must be realized through the refund procedures following purchase of the fuels tax-paid.

2. The Intercity Bus Industry and the Diesel Fuel Excise Tax Collection Process

While the ABA supports efforts to improve the efficient administration and collection of the diesel fuel excise tax, we maintain that the diesel fuel excise tax collection process has adversely affected the intercity bus industry.

Historically, Congress has encouraged the use of private intercity bus transportation. The Energy Tax Act of 1978, the

Highway Revenue Act of 1982, and the Tax Reform Act of 1984 all contained provisions exempting intercity buses from all or a part of the diesel fuel excise tax as well as other highway user taxes. This national policy stems from Congressional recognition that the intercity bus industry plays a unique and vital role in our nation's transportation system.

Under the law and regulations in existence prior to the 1987 Budget Reconciliation Act, bus owners and operators were given the option of paying the excise tax as the fuel was actually used in a bus on the highway. This option was available if the fuel was delivered into the bus operator's bulk storage tanks. However, the new law requires that the excise tax be collected earlier in the chain of distribution. Bus owners who utilize the procedure allowing them to pay the tax as the fuel was used must now pay the tax earlier, when the fuel is purchased. After paying the tax, the bus owner or operator applies for a refund (or credit) for 12 or 15 cents of the 15 cents per gallon tax. ABA members have been experiencing extensive delays, up to several years, in receiving refunds and, in addition, are burdened by the paperwork required to process the application. Further, the ABA members receive no interest on funds held by from the Internal Revenue Service.

We submit that increased savings and efficiency could be achieved by requiring bus owners and operators to initially pay only the 3 cents tax which they are liable for and not have the

added burden of a claim for refund. In addition, such a move would eliminate the IRS' administrative burden of processing the claims for refund and the tax credit.

3. Private Intercity Bus Industry is in Precarious Financial Condition

Competition in the intercity bus industry has increased dramatically since the 1982 deregulation of the industry. For the fiscal year which ended June 30, 1987, compared to the same periods ending June 30, 1986, operating revenues declined 12.1 percent, and revenue passengers carried decreased 19.1 percent. Net income declined from $26.7 million to $8.4 million. ABA believes that any additional burdens on the cash flow position of the intercity bus operator will narrow the already small margin of profit of many carriers forcing them to reduce service or cease operations.

As Congress has acknowledged in the past, the intercity bus industry provides affordable, convenient transportation to more than 350 million passengers annually. In comparison with other modes of transportation, intercity buses carry far greater numbers of senior citizens, students, military personnel, and women. An income profile of intercity bus passengers reveals that 58 percent have annual family incomes of less than $15,000.

Further, private bus companies receive no direct federal subsidy, yet most compete routinely with federally-subsidized

entities such as Amtrak and the airlines. Amtrak is directly subsidized at a rate of approximately $35 per passenger. It is estimated that the current 12 cents per gallon diesel fuel excise tax exemption amounts to an indirect subsidy of only 8 cents per passenger for the intercity bus industry.

It should be noted that the 1987 Budget Reconciliation Act gave the Treasury discretionary authority to exempt certain sales from tax. One of these is the sale of fuel for use by a state, a political subdivision of a state, or the District of Columbia. ABA submits that exempting publicly owned buses while requiring the private bus operator to pay the tax up front would further harm the competitive position of the private intercity bus industry vis-a-vis public transit authorities. Public transit authorities are increasingly competing with private bus companies on commuter routes and in charters and tours. They enjoy tax exemptions due to their status as governmental entities and they also receive federal subsidies. Publicly owned transit systems have received more than $1 billion annually from the Highway Trust Fund derived from taxes imposed on private highway users, including private intercity bus companies.

We understand that the Treasury Department is currently studying how to exercise its authority with respect to the diesel fuel excise tax and the possible exemption of state and local governments from the burden of having to pay the tax up front and then file for a refund. The American Bus Association urges that

similar action should be taken with respect to the private intercity bus industry.

Conclusion

ABA submits that the current procedures requiring intercity bus companies to pay the diesel fuel excise tax up front and file for a refund or credit are discriminatory. The cash flow problem caused by these procedures seriously endangers America's vital bus transportation network. ABA urges the Subcommittee to recommend that the procedures for collection and payment of the excise tax be revised to reflect the true exemption of the intercity bus industry from a portion of the diesel fuel excise tax.

MAR 0 8 1988

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Joseph Farrell
President

March 4, 1988

Hon. Charles F. Hatcher
Chairman
Subcommittee on Energy and Agriculture
House Committee on Small Business
Washington, D. C. 20515

Dear Mr. Chairman:

I am writing to contribute to the hearing record on certain serious inequities associated with the collection of diesel fuel taxes by wholesalers as prescribed by the Omnibus Budget Reconciliation Act of 1987 (P.L. 100-203). This communication is made on behalf of the American Waterways Operators (AWO), the national trade association for the coastal and inland barge and towing industry. Over one half the onboard jobs in the U.S. Merchant Marine have been created by the towing industry. In a typical year, there are one 125,000 moves to and from over 200 U.S. cities; 87 percent of all U.S. cities are served by tug barge moves. Almost 60 percent of grain exported by the United States is moved to seaports in barges, and one ton of every 5 tons of coal produced in the nation is carried by barge. Our vessels carry about 15 percent of the nation's intracity freight for just 2 percent of the total freight bill.

It is a supremely competitive industry. It is also the safest mode of transportation by any measure.

Fierce competition is the chief hallmark of this industry which produces a bounty for American shippers and consumers: quality service, innovation and, most of all, low prices. Thus, margins tend to be razor thin in the best of times. The line between survival and bankruptcy is always very narrow for barging companies.

In other words, anything which disturbs the thin margins threatens the existence for barge companies. And, the 15 cent per gallon tax on diesel fuel for Highway Trust Fund purposes, collected at the wholesale level beginning on April 1, 1988, takes dead aim at the barge industry.

Clearly, Congress did not intend that commercial waterway operators be asked to pay a tax they are not statutorily liable for. Our industry was simply caught up inadvertently in the noble effort to streamline collection of the tax and barricade against cheaters. Congress signaled its actual intent by exempting the rail and commercial airline modes of transportation, overlooking the water transport industry; diesel fuel for this industry cannot be diverted to highway use of any kind.

While the towing industry is eligible for a rebate of the fuel tax since the industry is exempt from the highway use tax, the upfront payment requirement will nonetheless impose staggering problems on the industry. Informal discussions with the Department of the Treasury indicate that as much as 18 months will elapse from the date of refund application to the date of refund of the rebate check. Or, that the barge industry will be floating a $360 million loan to the Federal government! Congress must view this massive loan from the private sector as constituting fully 20 percent of the industry aggregate annual revenues! A majority of barge companies have indicated that their quarterly excise tax payments now exceed their quarterly corporate income tax payments ... in fact, many of these companies are operating at no profit whatsoever.

The situation is nothing short of ridiculously unreasonable. It cries out not just for routine correction, but for Congress to expedite righting the wrong that it inadvertently created: if the statute cannot be amended in time to halt collection of the tax from the barge industry beginning April 1, then we urge the Congress to communicate to the IRS its intent to make the correction and ask the IRS to instruct diesel fuel wholesalers not to pass on to water carriers.

AWO appreciates the opportunity to submit comments for the record on this urgent matter, Mr. Chairman. We are prepared to assist the Congress in any way it wishes to help resolve the issue.

Sincerely,

Joseph Farrell

DEPARTMENT OF THE TREASURY
INTERNAL REVENUE SERVICE
WASHINGTON, D.C. 20224

COMMISSIONER

JUL 21 1989

The Honorable Charles Hatcher, Chairman
Subcommittee on Energy and Agriculture
Committee on Small Business
United States House of Representatives
Washington, DC 20515

Dear Mr. Hatcher:

Enclosed are our responses to the questions you posed in your March 2 letter on the diesel fuel excise tax collection process. Accompanying the responses is our written statement for inclusion in the record.

We appreciate the opportunity you've given us to comment on this issue and apologize for our delay in responding. Our responses to your questions reflect the most current and complete information on policy and procedure regarding the collection of the diesel fuel excise tax.

If we can provide further information, please don't hesitate to contact Bob Longford of our Legislative Affairs Division. Bob's telephone number is 566-4128.

With best wishes, I am

Sincerely,

Bryan Slone
Assistant to the Commissioner
(Legislative Liaison)

Enclosures
Responses to the Chairman's questions
Commissioner's written statement

Internal Revenue Service Responses to
Chairman Hatcher's Post-Hearing Questions
Regarding Diesel Fuel Excise Tax Collection

Question 1

What is the liability threshold for receiving a refund from the IRS? How much does a purchaser have to pay in order to receive his/her money back at the year's end? How much tax does a purchaser have to pay in order to receive his/her money back at the quarter's end?

Answer

Section 6427(i) of the Internal Revenue Code and section 48.6427-3(a)(2) of the Manufacturers and Retailers Excise Tax Regulations provide the following rules:

-- A taxpayer who has $1,000 or more in refund due for the diesel fuel excise tax at the end of any one of the first three quarters of the calendar year may file for a refund on or before the last day of the first quarter following the quarter for which the claim is filed.

-- For the fourth calendar quarter, a taxpayer may claim any refund for the year on Form 4136, Computation of Credit for Federal Tax on Gasoline and Special Fuels, and attach this form to his/her income tax return. If the taxpayer is not an income tax filer (e.g., a partnership), then a refund claim can be made on Form 843.

-- A taxpayer who is due a refund of less than $1,000 for a quarter must wait until the end of the year to file a claim for credit or refund for the quarter, even though refunds of over $1,000 may be due in other quarters.

-- The $1,000 threshold must be met for diesel fuel. Gasoline and diesel fuel claims cannot be combined to meet the $1,000 threshold.

Question 2

Can these regulations be implemented by April 1? Does the IRS have the mechanism to implement these changes by April 1? When will the IRS produce proposed regulations for the diesel fuel excise tax collection process? When does the agency anticipate it will have the necessary forms designed, printed, and distributed to IRS district offices and others in the field?

Answer

Regulations

Notice 88-30 was released to the public by the tax services on March 3, 1988, and was published in the Internal Revenue Bulletin on March 28, 1988 (IRB 1988-13). This notice, which has the force and effect of a revenue ruling, gave preliminary guidance as to what the regulations will provide regarding the new law governing diesel fuel and aviation fuel taxes. The notice also provided guidance relating to the floor stocks tax imposed on fuel held on April 1, 1988.

Notice 88-44 and Announcement 88-64 were released to the public by the tax services on March 31, 1988, and published in the Internal Revenue Bulletin on April 18, 1988 (IRB 1988-16). Notice 88-44 supplemented Notice 88-30 by providing further guidance on the floor stocks tax. Announcement 88-64 amended Notice 88-30 to clarify the recordkeeping requirements for those making tax free sales of taxable diesel fuel and to provide additional guidance both on how to register as a purchaser of diesel fuel for use other than as a motor fuel and how to file and pay the floor stocks tax.

Notice 88-55, released to the public on April 26, 1988 and published in the Internal Revenue Bulletin on May 9, 1988 (IRB 1988-19), modified Notice 88-30 by extending the period under which certain persons will be deemed to be registered producers and thereby permitted to purchase diesel fuel tax free. The period has been extended through May 31, 1988.

The IRS plans to issue temporary regulations together with a notice of proposed rulemaking by cross-reference to the temporary regulations as soon as possible. These regulations will be effective April 1, 1988.

Implementation

For the most part, the IRS is using existing forms and procedures, with minor modifications, for the collection and refund of the revised diesel fuel excise tax. The only problem currently anticipated is the impact of an estimated 2 million

additional refund claims in FY 1988 requiring 432 staff years to process. Because this provision was enacted in December of 1987, no allowance was made in the IRS budget for FY 1988.

Forms

Notice 88-30 and Announcement 88-64, referred to in Answer 1 above, provide instructions to taxpayers on how to use existing Form 720 to report and pay the diesel fuel floor stock tax and on how to use existing Form 637 to meet the registration requirements of the new diesel fuel law for tax free purchases.

Form 720 has been revised for use in reporting the diesel fuel tax for the second calendar quarter of 1988. The revised form was distributed in May. Revised Forms 637 and 637A, relating to tax free sales of aviation fuel, will be developed later in the year when regulations governing the diesel fuel tax are issued.

Question 3

What is the current procedure for collecting the diesel fuel excise tax?

Answer

Prior to April 1, 1988, Section 4041(a)(1) of the Internal Revenue Code imposed a tax of 15¢ per gallon on any liquid sold for use in a diesel-powered highway vehicle. Section 4041(d) imposed a Leaking Underground Storage Tank (LUST) tax of 0.1¢ per gallon on the same sale or use.

Under section 48.4041-5(a) of the Manufacturers and Retailers Excise Tax Regulations, the tax on diesel fuel was imposed on the seller if the seller delivered the fuel into the fuel supply tank of a diesel-powered highway vehicle. When the seller delivered the fuel into a bulk storage tank, the seller was liable if the buyer gave the seller, before or at the time of sale, a written statement that the fuel was to be used for a taxable purpose. In other cases when the seller sold in bulk and the buyer used the fuel for a taxable purpose, the buyer became liable for the tax.

Generally, sales for resale were not subject to tax. However, under section 4041(n) of the Internal Revenue Code, retailers could make an agreement with their suppliers so that the suppliers would pay the tax on sale to the retailers. This provision was in effect between April 1, 1987, and March 31, 1988.

The diesel fuel excise tax was, and continues to be, reported on Form 720, Quarterly Federal Excise Tax Return, which is to be filed and any tax due paid by the last day of the month following the end of the calendar quarter. Taxpayers who were or are liable for over $2,000 of excise taxes reportable on Form 720 must make semimonthly deposits of taxes during the following quarter. These deposits are generally due 9 days after the close of a semimonthly period. Semimonthly periods are the first through the fifteenth and the sixteenth through the last day of a month.

Taxpayers were and continue to be required to make monthly deposits of the tax if they are not liable for making semimonthly deposits and are liable for more than $100 reportable on Form 720 for any month of the quarter except for the last month. The liability for the last month may be paid with the Form 720.

Question 4

Does the agency have the authority to delay implementation of these regulations? What does the agency plan to do in terms of bonding and registration requirements?

Answer

The IRS does not have the authority to delay, by regulations, the implementation of the collection procedures set forth in the statute. Section 10502(e) of the Omnibus Budget Reconciliation Act of 1987 provides that "the amendments made by this section shall apply to sales after March 31, 1988." As an administrative agency, the IRS must implement the statute as written.

Notice 88-30, as amended by Notice 88-64, sets forth the bonding and registration requirements that will be contained in the regulations. Bonding is covered in Section V of Notice 88-30. Generally, no bond is required of a state or local government, with respect to heating oil, or if the applicant has a satisfactory filing, deposit, and payment history in all areas of Federal taxation. Registration requirements are set forth in sections III and IV of the notice.

Question 5

How does the agency propose to define a "producer"?

Answer

Section III(B)(1)(a) of Notice 88-30 states as follows:

"Section 4092(b) defines 'producer' as a person who is a refiner, compounder, blender, or wholesale distributor of a taxable fuel, or a dealer selling any taxable fuel exclusively to producers of such taxable fuel, and who elects to register under section 4101 with respect to the tax imposed by section 4091. The term, 'wholesale distributor' includes any person who sells a taxable fuel to producers, retailers, or to users who purchase in bulk quantities and deliver into bulk storage tanks. The regulations will provide that a wholesale distributor who also sells taxable fuel at retail may nonetheless qualify as a wholesale distributor under the statutory definition."

Question 6

How does the agency propose to define "off-road use"?

Answer

Section 4041(b)(1) provides an exemption from the diesel fuel excise tax for "off-highway business use" as defined in section 6421(e)(2). Section 6421(e)(2) and regulations at section 48.6421-4(b) define "off-highway business use" as any use by a person in a trade, business or income producing activity other than as a fuel in a highway vehicle that is registered or required to be registered for highway use by the laws of any State or foreign country, or that is owned by the United States and is used on the highway. The term does not include use in a motor boat other than a vessel used in the fisheries or whaling business. This definition will continue to govern sales of liquid fuels taxable under section 4041 and refunds or credits of tax paid with respect to fuels taxable under section 4091.

Question 7

Since the new tax collection process would require the off-road user to deal with more paperwork, i.e., additional tax forms, etc., is the possibility for tax fraud increased? Why or why not?

Answer

We do not believe the paperwork for the off-highway user would increase or decrease the possibility for tax fraud. Prior to April 1, 1988, off-highway users who purchased diesel fuel tax free were required to keep track of all such fuel put to highway use so they could file a return and pay the excise tax on that fuel. Under the new law, off-highway users must purchase diesel fuel tax-paid and keep track of off-road use so they may file a claim for credit or refund. Therefore, the amount of paperwork should remain about the same.

Under the prior law, the off-highway user who purchased diesel fuel tax free in bulk was responsible for reporting on Form 720 the amount of such fuel used in a highway motor vehicle and paying the applicable excise tax. Noncompliance occurred whenever the amount of fuel purchased tax free but put to taxable use was either not reported or underreported. Tax fraud occurred whenever such nonreporting or underreporting was a knowing and deliberate failure to comply with the law. The difficulties of detecting noncompliance under this system were compounded by the large number of taxpayers involved. Further, to recover unreported taxes, the Service had to first discover the underreporting, determine the extent of the underreporting (often in the absence of books and records from the taxpayer), propose and assess the appropriate tax liability, and, ultimately, collect the additional tax, penalty, and interest associated with that assessment.

Under the new law now in effect, Congress sought to curb the potential for noncompliance by eliminating the provisions for tax free purchases below the producer level. Therefore, the off-highway user is no longer able to purchase tax free and must claim a credit or refund of the tax. While fraudulent claims for credit or refund may be made, the Service's examination programs will be reviewing such claims from many taxpayers and will now be able to examine the taxpaying claimants books and records to verify the accuracy of those claims. That means that attempts at noncompliant behavior will be more likely to be detected, the extent of any noncompliance will be easier to determine, and the collection of legitimately owed taxes will for the most part already have taken place.

Consequently, as long as IRS has adequate funding to examine claimant books and records at a reasonably high rate, the possibility of tax fraud in off-highway situations can be expected to diminish significantly -- not to increase.

Question 8

How is the state and local government exemption for refunds going to work on a case-by-case basis?

Answer

Requirements relating to the allowance of tax free sales of diesel fuel and aviation fuel by a producer to state or local government are set forth in section IV(G) of Notice 88-30. Generally, a tax free sale to a state or local government will be allowed if the government provides the seller with a certification that fuel purchased tax free is for the exclusive use of the government.

If a state or local government purchases taxable fuel from a retailer and pays a price for the fuel that includes the tax imposed under section 4091, the state or local government may claim a refund of the tax paid as would any other purchaser who uses taxable fuel for a nontaxable purpose. This procedure is described above in the answer to Question 1.

Question 9

How much will it cost the government to implement this new collection process?

Answer

Based on a projected 2 million diesel fuel claims to be filed annually, the cost of processing those claims would come to $8.4 million. The related examination costs, including registration and bonding, would be another $22.6 million. Consequently, the total estimated annual cost for the two most cost-significant administrative areas is $31 million.

Question 10

Does the agency have plans to add diesel to items which are considered for exemption on a case-by-case basis?

Answer

The IRS has no authority to grant any exemption from the tax imposed under section 4091 except as specifically provided under section 4093 of the Code. Guidance has been issued providing the fullest exemptions possible within the limits of section 4093. However, if Congress adds further sales or uses of fuel to the exemptions permitted under section 4093, we will issue additional guidance relating to those exemptions.

Question 11

Were alternate changes in the diesel fuel excise tax collection process considered? If so, what were their potential savings or costs?

Answer

No alternate changes in diesel fuel excise tax collection were considered, at least to the extent that potential cost and savings estimates were developed for those alternatives.

Question 12

Has the agency considered allowing states to collect the federal tax on diesel? What are the potential advantages or disadvantages of this proposal?

Answer

The idea that states could assist in collecting federal excise taxes imposed on diesel fuel has been in circulation for a number of months. The possibility was raised formally to us by the former Federal Highway Administrator Ray Barnhart and is still under consideration.

Question 13

Has the agency considered collecting the excise tax on diesel separate from other excise taxes? Has the agency considered modifying the 720 form?

Answer

The Service has considered a separate fuels excise tax form as opposed to a form unique to diesel fuel only. Because of the costs of processing a separate tax return, this idea was rejected in favor of enhancing the existing Form 720, Federal Excise Tax Return, which is currently used to report fuels taxes and other excise taxes. The Form 720 has been redesigned to provide for reporting of total volumes, sales, and amounts needed to compute the tax for each type of fuel.

In order to make the Form 720 as simple as possible for most filers to use, we are working on an attachment to the form that will capture valuable additional information pertaining to all taxed fuels. The attachment would be filed with the Form 720 very much the way special schedules (e.g., Schedule B), are attached to individual taxpayers' Forms 1040. This attachment is planned for use with the first quarter Form 720 for 1989.

Statement of
Lawrence B. Gibbs
Commissioner of Internal Revenue

Before the
Subcommittee on Energy and Agriculture
House Small Business Committee

March 10, 1988

Mr. Chairman and Members of the Subcommittee:

I am pleased to have the opportunity to present written testimony regarding the recent legislation affecting the collection of the federal excise tax on diesel fuel. The Internal Revenue Service is sensitive to the impact of this new legislation on small businesses and farmers. To the extent allowed by law, we have considered their concerns in the implementation of this legislation.

In my testimony, I would like to address three key points:

(1) When Congress enacted the new diesel fuel excise tax provisions as part of the Revenue Act of 1987, the law was drafted without a specific exception to the new collection and refund process for farmers or small businesses.

(2) There have been significant compliance concerns with respect to the current collection system which were the basis for the legislative change.

(3) If Congress decides to reconsider the applicable provisions in the Revenue Act of 1987, we would hope that these compliance concerns would be addressed in any amendments. In this regard, we would be pleased to work with Congress and the Department of the Treasury to evaluate alternative proposals.

I. The New Law

As part of the Revenue Act of 1987, Congress changed the collection procedures for the diesel fuel excise tax. Beginning April 1, 1988, collection of the excise tax is required upon the sale of diesel fuel by wholesale distributors or other intermediate persons in the diesel fuel distribution chain. In other words, this tax is now generally imposed at the wholesale level. Moreover, even for persons at the wholesale level to purchase diesel fuel tax free, they must satisfy certain registration and bonding procedures recently published by the Internal Revenue Service in Notice 88-30. The registration and bonding requirements as well as the movement of the collection point of the excise tax to the wholesale level are the two major changes to current law.

Prior to the April 1 effective date of the new law, the excise tax was imposed when the fuel was delivered by a retailer into a diesel-powered highway vehicle. Thus, anyone (including truck stops, farmers, and construction companies) purchasing diesel fuel to be put into storage tanks (as opposed to a highway vehicle) was able to do so tax free. It was only when the fuel was subsequently transferred to a diesel-powered highway vehicle from such a storage tank that a liability was incurred and the tax was required to be reported and paid. If a subsequent use was tax-exempt, no reporting or

remittance of tax was necessary. Such uses included use in off-highway vehicles, on a farm for farm purposes, for vessels and aircraft, and for the exclusive use of any state, political subdivision of a state, or the District of Columbia. Under the new law, however, such exemptions from the excise tax generally have to be realized through refund procedures following the purchase of the fuels tax-paid.

The new law provides the Department of the Treasury with discretionary authority to exempt certain sales from the tax. This authority, however, extends only to sales of (1) aviation fuel sold for use as a fuel in an aircraft in commercial aviation, (2) diesel fuel sold for use as fuel in a diesel-powered train, (3) fuel sold for industrial use other than as motor fuel, and (4) fuel sold for the exclusive use of any state, a political subdivision of a state, or the District of Columbia. Sales of fuel that Treasury determines is destined for use as heating oil are also exempt from tax. Guidelines regarding the implementation of the exemption provisions are also contained in Notice 88-30. The Treasury does not have the authority to exempt sales of diesel fuel to farmers or small businesses unless the sales to small businesses specifically come within one of the above discretionary exemptions.

II. Compliance Concerns

In recent years, the economic incentive to evade diesel excise tax has become greater, because the diesel excise tax rates have increased. As recently as 1983, the federal excise tax on diesel fuel was only 4 cents a gallon. On April 1, 1983, the rate was increased by Congress to 9 cents a gallon. One year later, another increase by Congress raised it to 15 cents a gallon. Coincidentally, many states and localities, faced with their own demands for highway improvements, also increased their excise taxes imposed on the sales of these fuels. In at least one case, combined tax levied at the federal, state, and local levels now exceeds 35 cents a gallon.

From a compliance point of view, the old law was difficult to enforce. As previously mentioned, anyone could purchase diesel fuel tax free as long as it was not delivered by the seller into the purchaser's diesel-powered highway vehicle. Thus, if a wholesale distributor instead delivered diesel fuel to a purchaser's storage tank, the potential for abuse was significant from that point on in the distribution chain. A 1985 cooperative federal/state exchange excise tax project, involving twenty-five taxpayers, revealed that the diesel fuel excise tax was incorrectly reported on 65% of the 128 returns examined. Estimated additional tax and penalties for these

cases totalled $1,832,781. The audit coverage for this project included truck stops, wholesale distributors and trucking companies.

By moving the point of collection to the wholesale level, there will obviously be fewer opportunities for abuse. Also, the universe of those charged with remitting the tax to the federal government, it is estimated, will decrease from approximately 60,000 to somewhere between 15,000 to 20,000 taxpayers. Such a contraction in the number of collection points will allow a corresponding increase in IRS' audit coverage for this tax.

The legislation, however, will have a paperwork impact. Eliminating many sales that were previously tax free, while at the same time continuing the exemptions from tax for many uses, imposes certain reporting requirements on taxpayers and processing demands on the IRS. There is also the cash flow consequence to those purchasers who presently use the fuel for a tax free purpose, such as farmers.

III. Policy Concerns If Changes Are Again Made

If Congress revisits this legislation, the economic impact of the new legislation on the farmer or small business person must be weighed against the overall compliance benefits. The

amount of revenue collected from the diesel fuel tax is significant and any improvement in compliance offers the opportunity to collect meaningful amounts of additional new revenue without increasing tax rates. During fiscal year 1985, diesel and special motor fuel collections amounted to $2,430,165,000, and in fiscal year 1986, $2,613,918,000.

On the other hand, the new provisions will have an economic impact on farmers and small businesses. Let me use the small farmer as an illustration. Based on data the IRS received from the Department of Agriculture (Office of Energy), the impact on most farmers will be less than $400. Of 1,319,351 existing farms surveyed in 1982, 1,048,652 or 79% will now have to pay, on an annual basis, an average diesel fuel excise tax ranging from $36 to $347 before receiving a refund or credit of a like amount.

IV. Summary

From an overall perspective, the changes to the diesel fuel excise tax address valid collection considerations. Certain aspects of the new legislation, however, have sparked controversy and may warrant further study. The Service stands ready to discuss with your subcommittee, and any other, constructive alternatives to ease these concerns. Care should be taken to safeguard the well-intentioned compliance measures of this legislation.

I appreciate the opportunity to provide these comments to you.

STATEMENT

of

GOVERNMENT FINANCE OFFICERS ASSOCIATION

before the

COMMITTEE ON SMALL BUSINESS
SUBCOMMITTEE ON ENERGY AND AGRICULTURE
UNITED STATES HOUSE OF REPRESENTATIVES

March 31, 1988

The Government Finance Officers Association represents over 11,000 state and local government officials, including purchasing and budgeting officials, and other finance professionals involved in all aspects of government finance. We are submitting this testimony because the federal excise taxes on gasoline and diesel are causing difficulties for governments at all levels, even though the governments are exempt from the taxes.

A Hidden Tax

Before the Tax Reform Act of 1986, states and localities were exempt from paying the federal excise tax on gasoline just as federal vehicles were exempt from state and local fuels and vehicle taxes. The Tax Reform Act did retain the exemption for states and localities, but it prohibited tax-free sales. Thus, states and localities, even though exempt, must pay the tax, and then seek a refund from the federal government. Meanwhile, the federal government continues to be exempt from the state and local taxes.

Clearly, the most seriously affected governmental units are police, fire, and other public safety departments. This is especially true since many of them were in the middle of their budget year when the refund provision became effective.

In actuality this so called exemption creates a hidden tax - states and localities lose money on the bookkeeping and administrative costs they incur while tracking the amount of tax paid, and they lose the use of the tax money while the

federal government holds it.

Moreover, while states and localities are losing the use of this money, others are using it interest-free. The refiners and terminal operators have the use of the money until they remit it to the federal government.

Furthermore, the law does not set a time period within which the federal government must make the refund, thus creating cash flow problems for states and localities. Cash flow problems will also result from the rules governing when a government can apply for a refund. Only if $1000 or more is paid in tax during a quarter can a refund be filed immediately after the close of the quarter. Otherwise the refund must be requested annually. This delay puts smaller towns at a disadvantage and causes them to lose the use of those dollars - sometimes for a year or more.

A sampling of state and local entities illustrates the severity of this loss of cash flow:

- In Oklahoma, Oklahoma City, with a population of 445,799, uses 1,592,000 gallons of gasoline and will pay approximately $145,000 in tax. Tulsa has 360,919 residents, uses 1,742,072 gallons, and will pay $158,528 in tax. McAlester, with 18,418 residents uses 100,000 gallons and pays $9,100 while Grove, with 4055 residents, uses 16,000 gallons and pays approximately $1450 in tax.
- The state vehicles for the State of Wyoming use 3.5

million gallons of gasoline, costing the state $318,500 in tax.

- South Dakota's state fleet uses 600,000 gallons of gasoline and pays tax of $54,600. This does not include the highway patrol.
- In Hawaii, the City of Honolulu uses 2,525,000 gallons of gasoline, which costs the city $229,775 in taxes.
- The Colorado Department of Education, with 176 school districts and 4700 school buses that travel 55.5 million miles to cover those districts, will use an estimated 12 million gallons of gasoline a year. The $1.1 million tax paid is considered a liability on the Department's books and so it cannot be used for educating students until it is returned by the federal government.

It's Going to Cost the Federal Government Too

One of the drawbacks of not giving this provision more consideration is that there are approximately 83,000 state and local governments and special districts that are eligible to apply for refunds. With a number of governments eligible to make quarterly filings because they pay $1000 or more of tax in a quarter, there could be upwards of 200,000 annual filings for refunds. The federal government will have to pay for this refund process.

Administrative Costs

Earlier I mentioned there were administrative costs for states and localities paying the tax and seeking the refund. It is important that you know what that entails.

First, someone has to keep track of how much tax has been paid. This presents a problem for small towns which have few or no full-time staff to file the refund or to follow-up to assure that the refund is received. Larger counties and cities that have staffs will have to increase their number of employees to accommodate the refund procedure. Someone has to keep track of the gasoline that all those departments purchase. The department of public works buys gasoline, the fire department buys gasoline, the police buy gasoline. Even libraries buy gasoline so they can have their bookmobiles go to people who might not otherwise be able to get books.

It would be easier if each department were able to apply for its own refund, but the IRS has told us that every department or section of government that uses the same Employer Identification Number (EIN) for taxpayer purposes must file for a refund on the same form. This creates a major problem. For example:

o In Maryland, all state departments, from the Department of Natural Resources to the University system use the same EIN, thus the state may use only one form to file for the refund for the tax paid by the entire state.

Maryland is not alone with its problems:

- California is investigating three options to deal with the tax:
  1. Establish a separate office to centralize the refund procedure for the state's 300 agencies and departments.
  2. Have the departments that are major users of gasoline obtain their own Employer Identification Numbers.
  3. Renegoiate the the contracts the state already has with 41 gasoline vendors to have them sell the gasoline tax-free to the state. This would put the financial burden on the vendors, a number of whom are minority-owned firms.

Each of these options would cost the state time and money.

- In South Carolina, a change in state law is necessary in order for a state agency to receive its share of the gas tax refund when the refund is received in a different state fiscal year than the year the expenditure was made.

<u>If Evasion Is The Problem Enforcement Should Be The Solution</u>

I understand the motive for changing the point of collection of the tax was to avoid evasion. We support these efforts. Preventing tax evasion helps law-abiding taxpayers, as well as those of us who share in the benefit

from the tax. However, we were exempt so had no reason to evade paying the tax, and neither the Treasury or the Congressional Research Service reports suggest that states and localities were responsible for the evasion problem. Stronger enforcement of the existing laws would have made more sense than putting the collection burden where it does not belong.

Section 6416, Limited Relief

An existing portion of the Internal Revenue Code, Section 6416, provides limited relief to states and localities, but it is clear that it does not help everybody. Because wholesalers and refiners voluntarily use this provision, state and local governments are at their mercy. Moreover, small governments that are more likely to purchase gasoline at the retail level are not helped by this section unless they purchase gasoline using a major oil company credit card and then only if the company has opted to use Section 6416.

Section 6416 allows wholesalers to sell tax-free to states and localities. But the wholesaler must have the agreement of the ultimate taxpayer - the refiner or terminal operator. While some refiners are honoring wholesalers' requests to sell tax-free, others are not. This puts governments in the position of having to pay the tax, or shop around for a supplier who is able sell tax-free. Moreover,

there is concern that gasoline prices will rise because wholesalers that waive the tax will want compensation for their paying the tax and waiting for a refund.

One way to alleviate the problem is to adopt the "Pickle Amendment" contained in the House technical corrections bill, which would allow the wholesaler to offer tax-free sales to qualified purchasers without the permission of the refiner. The retention and stengthening of Section 6416 would allow wholesalers to act independently and stimulate competition.

As important as Section 6416 is to many state and local governments it is still not a complete solution. Some governments and wholesalers don't know about it. Many are not in an area of the country where there is enough competition between wholesalers to make 6416 a factor. Others are too small to have the clout to receive the benefits of 6416. These small governments can ill afford to pay the tax and wait an unknown period of time for the refund.

Solutions

Restore True Exemption

Changing this tax paying and refund procedure to the more sensible exemption that was previously in place is simple enough that it could be part of the technical corrections to the Tax Reform Act of 1986. Or it could be done through separate legislation that Senator Nickles has

proposed in S. 2062 and Congressman Neal has proposed in H.R. 3892.

In addition, Senator Daschle has introduced S 2075 that would provide an administrative mechanism that would allow state and local governments to purchase diesel fuel tax-free. We support Senator Daschle, as well as the Chairman of this Subcommittee, Senator Boren, and the members of the Finance Committee who are co-sponsors in this effort. This approach is a good beginning but incomplete. As the Committee moves to mark-up, we recommend that you address a comprehensive approach to the diesel and gasoline fuel excise tax burdens on states and localities.

Diesel Option

An alternative solution for gasoline would be to set up a system similar to the one that Secretary Baker has proposed in Internal Revenue Notice 88-30 concerning diesel where, upon receipt of certification from a state or local government, the wholesaler or refiner would sell tax-free and be able to receive a credit or refund. We commend the Secretary and the IRS for proposing a system that will greatly ease the burden on states and localities. The Notice says that states and localities will not be required to register or to pay the tax on diesel fuel they buy which has not already had the tax imposed. This is likely if they purchase from a registered wholesaler. If they purchase

after the tax has been imposed, and themselves pay the tax, they can apply for a refund.

It appears that this system will be workable. However, as with Section 6416 with gasoline sales, it will not benefit the smaller governments - those who do not purchase enough diesel to merit having their own storage tanks and must buy retail, pay the tax and apply for a refund.

Conclusion

The refund procedure is a costly and unnecessary burden on taxpayers, states and localities, and the federal government. State and local governments have not abused the exemption, and should not have to bear the cost of combatting the evasion. Therefore a return to a true exemption is warranted.

Questions can be directed to Cathie Eitelberg or George Elser of GFOA's Federal Liaison Center, 1750 K Street, N.W., Suite 200, Washington, D.C. 20006 (202-429-2750).

NATIONAL COTTON COUNCIL OF AMERICA

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FAX: (202) 331-0622

March 2, 1988

The Honorable Charles Hatcher
Chairman
Subcommittee on Energy & Agriculture
House Annex 2
Room 569
Washington, D.C. 20515

Dear Mr. Chairman:

The National Cotton Council is the central organization of the cotton industry, representing producers, ginners, seed crushers, warehousemen, merchants, cooperatives, and textile manufacturers in 18 cotton producing states. On the average, our crop covers some 12 million acres with annual cotton production at approximately 13 million bales. In a typical year, U.S. cotton producers invest more than $300 million in fertilizer, $500 million in agricultural chemicals, and $450 million for fuel and equipment. All together, business revenues stimulated by cotton in the nation's economy are estimated at $45 billion, the largest of any U.S. crop.

The National Cotton Council wishes to take this opportunity to congratulate you and the members of your committee for holding a hearing on March 3, 1988 on the effects of the change in the collection point for the 15 cents per gallon diesel tax. As you and the members of your committee know, the change in the collection point for the diesel tax from the retail level to the wholesale level has been one of the most controversial provisions of the Omnibus Budget Reconciliation Act of 1987. The effect of this change is to require farmers who are exempt from the tax for off-highway use to pay the tax on purchase and then file for a refund or credit.

Our specific concerns with the new tax provisions are:

1. Since farmers are exempt from the diesel tax for off-highway use, it seems totally unnecessary to require payment of the tax and then have producers file for a refund or tax credit

2. Higher interest costs and cash flow problems will undoubtedly result from the new tax collection procedure and individual producers must increase their operating loans to cover taxes ranging from several hundred to several thousand dollars. Based on the 1982 Census of Agriculture, annual diesel fuel use is probably three billion gallons per year. At 15 cents

per gallon, the annual diesel tax collection could amount to $420 million. This is a substantial figure for which production finances would be required up front. Interest on this money would obviously increase the cost of agricultural production.

3. The Internal Revenue Service does not pay interest on the tax held prior to refund. This amounts to an interest free loan by farmers to the federal government, and we find this an unacceptable practice.

4. In addition to the added paperwork costs to farmers, the costs to the Internal Revenue Service of distributing and maintaining a refund system will possibly outweigh the benefits of any added revenue which may find its way to the Treasury.

Several bills have been introduced to date that would permit farmers to continue purchasing diesel tax-free for off-highway use. While the legislative language of these bills may vary to some extent, each of them will accomplish agriculture's goal of continuing farmers' tax-free purchase of diesel fuel for off-road use.

In summary, the National Cotton Council is requesting that you and the members of your committee support legislation that will permit farmers to continue to buy diesel fuel tax-free if it is used for off-highway purposes. We would further urge that any revenues lost through repeal not be recaptured through the imposition of new taxes on the agricultural sector.

Again, we congratulate you and the members of your committee in scheduling a hearing to listen to our concerns.

Sincerely,

Earl W. Sears

Earl W. Sears
Executive Vice President

EWS/jlc

March 8, 1988

National
Council of
Farmer
Cooperatives

The Honorable Charles Hatcher
Chairman
Subcommittee on Energy and Agriculture
Committee on Small Business
United States House of Representatives
Washington, D.C. 20515

Room No. H2-569
House Annex 2

RE: DIESEL FUEL EXCISE TAX COLLECTION PROCESS

Dear Mr. Chairman:

The National Council of Farmer Cooperatives (National Council) is pleased to submit comments concerning changes in the diesel fuel excise tax collection process as they impact upon the American farmer.

Interest of the National Council

The National Council is a nationwide association of cooperative businesses which are owned and controlled by farmers. Its membership includes 91 major marketing and farm supply cooperatives, the 37 banks of the Farm Credit System, and 33 state councils of farmer cooperatives. National Council members handle practically every type of agricultural commodity produced in the U.S., market these commodities domestically and around the world, and furnish production supplies and credit to their farmer members and patrons. Five out of six U.S. farmers are affiliated with one or more cooperatives. The National Council represents about 90 percent of the nearly 5,800 local farmer cooperatives in the nation, with a combined membership of nearly 2 million farmers.

Among the farmer cooperatives the National Council represents are supply cooperatives which own and operate five efficient refineries possessing an aggregate production capacity of 337,700 barrels per stream day. Cooperatives market petroleum products in more than 40 states and currently supply about 40 percent of all on-farm fuel and a large portion of rural needs.

Farmer cooperative petroleum operations represent the only segment of the oil industry in which the consumers of its products are also its owners. This feature carries with it a unique accountability in terms of commitment of supply, service and price.

50 F Street, NW
Suite 900
Washington, DC 20001
202/628-6676

Serving America's Family Farmers

The Problem

The American farmer has been able to make tax exempt purchases of diesel fuel for farm operations and other off-highway uses ever since the highway use tax at the federal level was established.

When Congress enacted the Budget Reconciliation Act, it included a provision that moved the point of taxation from the retail level to the last wholesale level. As we understand it, the objective was to reduce or eliminate tax evasion, particularly at truck stops. Congress also eliminated a number of exempt purchase categories, including that for farmers, while allowing the IRS to continue exemptions on a case-by-case basis for railroads, airports and state and local governments. There is no such discretionary authority for the farm community.

This change means that farmers will have to pay the excise tax on all diesel fuel purchases, regardless of intended use, effective April 1, 1988--absent timely action by the Congress and/or the IRS. The price paid will increase by 15 cents per gallon. Should states mirror the federal legislation in their tax collection practices, as expected, the total retail price increase could be up to 25 cents per gallon.

Farmers will have two basic options for reimbursement of taxes paid which they do not owe:

1. A credit on one's income tax return (1040); or

2. A direct refund, up to a quarterly basis over the first nine months of any year, if the liability exceeds $1,000.

In economic terms, this means that the IRS is securing an interest free loan from farmers, starting from the time the tax is paid to the point at which a refund or credit occurs. Realistically, only the larger farms will have the option of exercising the direct refund option. In most instances, cash that is badly needed to defray ongoing expenses of farm operation, or of farm family needs, will be transferred from farmers to the coffers of the IRS. Depending upon one's assumptions, the time cost of money denied farmers could range from $6 million to $25 million annually.

The National Council anticipates that the local cooperative will qualify as a wholesaler for the purpose of assessing the highway use tax on diesel fuel, in that local cooperatives make bulk deliveries to storage tanks of farms. Local cooperatives have also served as the retailer responsible for collecting the same excise tax under laws in effect up to this point. Thus,

the new tax change is expected to have only minimal effect upon the cooperative petroleum supply system. Over the years, we believe that cooperatives and their farmer customers have established a good track record in distinguishing between off-highway (exempt) use of diesel fuel and those purchases for on-highway transportation. Indeed, the IRS recognized in proceedings last year that the recordkeeping system of petroleum cooperatives at self-service, "Cardtrol/Keytrol" stations had sufficient quality control to permit both taxable and nontaxable sales to farmers through those outlets.

Thus, the National Council does not believe that the congressional objective of reducing tax evasion—an objective which we wholeheartedly support—would be furthered in any way by forcing farmers to pay a tax which they do not owe on their major power fuel, and then seek a credit or a refund subsequently. The major impact of this new procedure is more likely to be a paperwork nightmare for both the farm community and the IRS. The dollar costs of that burden surely would more than cancel out any diminimus improvement possible in tax collection.

Recommended Action

Accordingly, the National Council would urge the Congress to act swiftly to restore the farm exemption from the highway use tax on diesel fuel as quickly as possible.

We hope that the IRS would immediately exercise any flexibility that it might possess under existing law to suspend the effective date of this change until such time as Congress can complete its work. It makes little sense for the agricultural community, the rural petroleum supply system and the IRS to go through the extensive time and costs involved in implementing this change, only to reverse the process a few months later.

We would respectfully request that this letter be incorporated as part of the record of the March 3, 1988 hearing before this subcommittee on the diesel fuel excise tax issue. The National Council and its members stand ready to assist in bringing this problem to a successful resolution.

Sincerely,

R. Thomas Van Arsdall

R. Thomas Van Arsdall
Vice President
Agricultural Inputs and Services

RTVA/kf

Statement of

The National Stone Association

Presented To The

Committee on Small Business

Subcommittee on Energy and Agriculture

United States House of Representatives

March 16, 1988

on the Topic of

The Repeal of the Up-Front Diesel Fuels Tax Exemption for Off-Highway Business Use

The National Stone Association represents 423 firms that produce crushed stone or manufacture equipment used in such operations. The crushed stone produced by our members is used in the concrete included in constructing our nation's buildings, highways, and industrial and municipal-utility facilities and in the asphalt for highways, parking lots, driveways, and walkways. A substantial portion of the crushed stone produced by NSA members is used for agricultural purposes, erosion control, railroad ballast and environmental applications. Stone, in short, is indeed a ubiquitous national resource.

The National Stone Association welcomes this opportunity to comment on the need for corrective action to restore the up-front diesel fuels tax exemption for off-highway purposes. NSA commends the Chairman and Congressman Combest for the leadership they have shown in holding these hearings and in introducing legislation that would restore the up-front diesel fuels tax exemption allowed under law prior to the passage of the Omnibus Budget Reconciliation Act of 1987.

Mr. Chairman, as an industry composed primarily of small firms, the repeal of the up-front diesel fuels tax exemption imposes a significant burden on crushed stone producers. The crushed stone industry is a capital and energy intensive industry which employs large bucket loaders, bulldozers and over-sized trucks that haul stone from the working face of the quarry to the primary crushers. All of these operations take place within the confines of the quarry; very few of our members own on-highway haulers, as most of them contract out such work to independent contractors.

Simply put, Mr. Chairman, under the law in existence prior to the Budget Reconciliation Act of 1987, only that diesel fuel consumed by on-highway vehicles was subject to the federal excise tax. Conversely, diesel fuel consumed in off-highway operations, such as construction, quarrying and agriculture, among others, was exempt from the tax.

The rationale for adopting this dichotomous approach lies in the principle of the user-fee system which serves as the funding mechanism for the Highway Trust Fund: that the users of the nations's highways, roads and bridges should pay a predetermined share of the construction and repair cost of this vital component of our infrastructure. Because off-highway uses do not contribute to the wear and tear of our roads and bridges, vehicles employed in such operations were totally exempt from the tax.

The Budget Reconciliation Act of 1987 changed the existing law by eliminating, effective April 1, the off-highway diesel fuels tax exemption requiring crushed stone producers to pay an up-front 15.1 cents per gallon diesel fuels tax to the federal Treasury. Following the payment of the up-front diesel fuels tax, these same producers will be allowed to recover the money paid into the Treasury after filing an application documenting that the fuel was consumed in a non-taxable use.

Mr. Chairman, it is apparent to us that the provision of law implementing this change was singularly ill-considered. The effect of the up-front diesel fuels tax on crushed stone producers is threefold: 1) it imposes an additional and

unforeseen production cost on existing supply contracts; 2) it will require additional record-keeping and paperwork to prepare the applications for refunds; and, 3) it will result in the loss of investment income or time value of the funds paid for the tax.

The impact of this change in the tax law on the cash flow of crushed stone producers is significant. For example, one of our member firms, B.L. Anderson, Inc. located in Iowa, used 266,844 gallons of diesel fuel in 1987 for off-highway purposes. The imposition of the 15.1 cents per gallon tax on this particular firm will result in a cash flow loss of $40,293 for that year. On existing contracts, this loss will have to be absorbed by the firm.

The proponents of the up-front diesel fuels tax argue that refunds will be provided by the Treasury Department and will therefore result in no hardship. However, it is very likely that the Department will adopt a quarterly refund schedule which is likely to result in processing delays and the retention of funds without any compensation for the loss of interest which could otherwise have been earned on these funds.

Mr. Chairman, NSA is aware and fully supportive of the need to close the loopholes in our tax laws that allow anyone to avoid paying the taxes they rightfully owe. However, the system adopted by the Budget Reconciliation Act strikes us as draconian and entirely unnecessary.

The Budget Act, by its own terms, requires firms to pay taxes for wholly legitimate non-taxable activities and to subsequently recover their monies through a yet-to-be established refund mechanism -- again without any restitution for loss of interest. The same Act, oddly enough, carves out four exceptions for diesel fuel used for locomotives, commercial aviation, industrial purposes or by states or political subdivisions thereof. For any of these categories, the Act empowers the Treasury to grant an exemption from the up-front diesel fuels tax following a case-by-case review.

Mr. Chairman, the National Stone Association takes strong exception to this approach and finds it repugnant to any sense of fair play that preferential treatment is given to activities in these four categories while it is denied to our industry and all others. Where is the equity in this? If the case-by-case exemption process is deemed to be a sufficient safeguard to the perceived potential for wrongdoing, it should be extended to all industries and not limited to a preselected few that have no superior claim of legitimacy for their particular non-taxable use.

In conclusion, Mr. Chairman, the National Stone Association urges Congress to take corrective action and restore the diesel fuels tax exemption for the crushed stone industry and for all others that have a legitimate non-taxable use. Again, Mr. Chairman, we applaud your leadership in this matter and we look forward to working with you and the members of the Committee on this pressing issue.

PACIFIC SEAFOOD PROCESSORS ASSOCIATION
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March 11, 1988

The Honorable Charles Hatcher
House Committee on Small Business
Subcommittee on Energy and Agriculture
405 Cannon House Office Building
Washington, D.C. 20515

Dear Congressman Hatcher:

I am writing on behalf of the member companies of the Pacific Seafood Processors Association. The Association is submitting this letter for inclusion in the record of your hearing on the collection of federal fuel taxes.

Pacific Seafood Processors Association (PSPA) is a seafood trade association representing the processors segment and its members account for about 85% of the processed seafood produced in the Pacific Northwest and Alaska. The Association has been active in this representation for 74 years. Member companies account for annual gross sales in the neighborhood of one billion dollars.

First, we would like to thank you, Congressman Hatcher, and the Committee for addressing this problem in a timely fashion. As seafood processors, we spend millions of dollars annually for fuel to operate fishing vessels, floating processors and tenders. Naturally, we have traditionally been exempt from paying the 15 cents per gallon federal diesel fuel tax since our operations fall into the "off-road" category. We were very alarmed when we learned of the change which had been made in the collection system as part of the 1987 Omnibus Reconciliation Act. Our industry is a major user of diesel fuel, with some of the larger vessels consuming up to 6,000 gallons per day. At this rate, the tax liability of our member companies becomes a significant part of their overall financial operating picture. Also, since fuel consumption accounts for a large percentage of the fixed costs of these firms, this additional tax presents very real cash flow problems. For the most part, the members of PSPA are not large companies. Virtually all have sales under $250 million annually. The lost use of capital, and the considerable added paperwork caused by this change are, therefore, obstacles we can ill afford at a time when we are striving to compete in the world market.

As an aside, we should also mention that this new system will be an even bigger burden on the tens of thousands of individual commercial fishing vessels around the nation. Many of their vessels are operated by single owner/operators and are small businesses in the most classic sense of the term. The fact is that, in all likelihood, neither the American business community nor the Internal Revenue Service are prepared for the paperwork onslaught posed by this new tax collection system.

Finally, we would like to make a point which differentiates our industry from most other "exempt" groups. It is an obvious but significant fact that our operations not only fall into the "off-road" category, they do not even take place on land. While there may be an argument over what percentage of time a farmer uses his truck on the highways versus on the farm, there can be no doubt that our vessels are permanent off-road users of diesel fuel. Additionally, most of our member companies have extensive operations in the North Pacific off the coast of Alaska. Many of the ports where we buy our fuel are only accessible by boat or airplane, and quite often, the entire "highway" system consists of a few miles of dirt road.

We hope that the Committee will take our comments into account as the review of this situation continues. It is very important to our industry that we be returned as quickly as possible to the status of being truly exempt from this financial and paperwork burden.

Sincerely,

Barry D. Collier

Barry D. Collier
President

cc: House Ways and Means Committee
Congressman Les AuCoin
Congressman Don Bonker
Congressman Rod Chandler
Congressman Peter A. DeFazio
Congressman Norman D. Dicks
Congressman Thomas S. Foley
Congressman Mike Lowry
Congressman John R. Miller
Congressman Sid Morrison
Congressman Denny Smith
Congressman Robert F. Smith
Congressman Al Swift
Congressman Ron Wyden
Congressman Don Young

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March 18, 1988

The Honorable Charles F. Hatcher
Chairman
Subcommittee on Energy and Agriculture
Committee on Small Business
U.S. House of Representatives
H2-569 House Office Building Annex II
Washington, D.C. 20515

Dear Mr. Chairman:

The Society of Independent Gasoline Marketers of America ("SIGMA") respectfully submits these comments for the record of the Subcommittee on Energy and Agriculture's hearing held on March 3, 1988 regarding the collection of Federal excise taxes on sales of diesel fuel.

SIGMA is a national trade association comprised of approximately 295 independent marketers and private-brand, chain retailers of motor fuels. SIGMA's members sell motor fuels in all 50 States, and their sales represent between 15 and 20 percent of the retail market for motor gasoline.

SIGMA's members do not produce or refine crude oil. Thus, they are entirely dependent upon third parties for their supplies of motor fuels. As a result, they have built their businesses based upon marketing efficiencies. Specifically, by innovation in such cost-saving techniques as self-service and high-volume/low-margin marketing, SIGMA's members have reduced the amount of fixed operating costs which must be recovered in the per-gallon selling price charged to consumers. These cost efficiencies have enabled them to compete effectively with their integrated supplier-competitors.

SIGMA respectfully suggests to the Subcommittee that Congress seriously consider repealing the provisions of the Revenue Act of 1987 (Pub. L. No. 100-203) ("the Act") which, effective April 1 of this year, will change the point of collection for the

Federal excise tax on diesel fuel. SIGMA believes that such action is necessary to: (1) alleviate the substantial hardships imposed upon the tax-exempt community which have given rise to Congressional concerns, and (2) avoid a significant increase in evasion of the excise tax on diesel fuel to the detriment of the Federal Government's revenues and legitimate competitors in the diesel fuel market.

The underlying justification for the changes in the system for collecting the excise tax on diesel fuel was to enhance the Federal Government's revenues by reducing tax evasion and by accelerating the collection of the tax, thereby enhancing the Government's "float" on these receipts. Unfortunately, the cost of accelerating the collection of the diesel fuel excise tax is likely to be borne primarily by entities for whom such costs represent a severe hardship. Moreover, it is SIGMA's belief that the change in collection procedures provided for in the Act will result in a significant increase, rather than decrease, in tax evasion.

SIGMA's conclusion that the new collection procedure for the excise tax on diesel fuel will result in a significant increase in tax evasion, and corresponding reduction in revenues, is based upon three factors: (1) all diesel fuel is home heating oil, (2) the amount of money which can be generated through tax evasion, and (3) the relative ease with which such transactions can be structured to frustrate traditional enforcement efforts. An understanding of these three factors will demonstrate why an increase in tax evasion is virtually unavoidable.

At the outset, Congress should recognize that all diesel fuel can be used as home heating oil. Specifically, the principal basis upon which the two fuels can be differentiated is the cetane rating of fuel qualifying as diesel fuel. In many areas of the country, pipeline specifications require that any No. 2 distillate fuel, including home heating oil, meet the cetane requirements for diesel fuel. Under such circumstances, the only way to know whether No. 2 fuel is home heating oil or diesel fuel (and thereby properly subject to tax) is to know how it is in fact used. Normally, this determination can only be made upon the sale to the end user.

The prospective enforcement problem which the change in collection procedures will induce is enormous. Specifically, there will be two obvious means by which to evade the excise tax on diesel fuel. First, a wholesale distributor can simply purchase product as home heating oil and sell it as diesel fuel. An unscrupulous distributor clearly will not report this activity, but instead simply pocket the excise tax. Second, an unscrupulous marketer can purchase diesel fuel on an exempt basis and then resell that product through a number of "shell" corporations. At some point in its passage through this "daisy chain," the product will be invoiced as "tax paid." Thereafter, it can be resold and the purchaser will be able to rely justifiably on the seller's representation. This second scenario is identical to the tax evasion daisy chains which were uncovered with respect to gasoline in the metropolitan New York City area. It is mystifying as to why Congress, having changed the gasoline excise tax collection system to avoid this problem, has altered the diesel excise tax collection system to recreate it.

There is no question but that the excise tax on diesel fuel has been the subject of evasion in the past. Basically, there were two types of retailers: (1) law abiding, and (2) tax evading. The Act's changes in the diesel fuel excise tax collection system have created a situation in which law-abiding retailers will be offered "deep

discounted" diesel fuel by disreputable marketers. Given the amount of money involved in the Federal excise tax on diesel fuel (15.1 cents per gallon), a disreputable marketer will be able to discount its product in sales to retailers substantially and still realize enormous profits. The sums which can be illicitly obtained by this method are of such a magnitude as to virtually guarantee that organized crime will involve itself in the process.

If SIGMA's fears are realized, then the anticipated revenue benefits of the change in the collection system will not be achieved. To the contrary, the Treasury will experience a loss of revenues. Moreover, the unlawful activity which will generate such losses will have a significant and detrimental effect on the competitive viability of legitimate marketers and retailers. Thus, the desired benefit will not be obtained and a clearly unintended injury to competition will be inflicted.

If Congress elects not to repeal the Act's changes in the collection procedure, at a minimum, it should amend the Act's definition of the term "producer" to include chain retailers within that definition. The Act's definition of the term "producer" essentially is identical to the definition of that term previously used in the gasoline excise tax collection system in all respects save one — it does not include chain retailers.

Chain retailers, i.e., firms which supply ten or more commonly-controlled outlets, perform all of the distributive functions performed by wholesale distributors. Specifically, they obtain the product and transport and deliver it to a retail distribution system. By excluding such firms from the definition of "producer," the Act imposes on these firms costs not imposed upon other entities with which they compete. Given the small number of firms which correcting this situation would add to the rolls of taxpayers, and the significant inequity which their exclusion creates, it is eminently reasonable to request that the Act's definition of "producer" be amended to include them.

Finally, it is important to communicate one general, but in SIGMA's view, enormously important observation. The changes in the systems for collecting the diesel fuel and gasoline excise taxes which Congress has enacted were to a substantial extent premised on an accurate view that the Treasury was losing funds to tax evasion. However, these changes have not closed off the possibility, and perhaps more appropriately the probability, of continued evasion. Moreover, while failing to achieve one of their primary objectives, they have generated significant hardships to law-abiding citizens. The saddest part of this reality is that Congress has available to it an alternative which would substantially reduce the possibility of tax evasion while creating minimum hardships for marketers and consumers of motor fuels. Specifically, Congress could provide the Internal Revenue Service ("IRS") funds for and direction to tie the motor fuels excise tax collection system into an electronic data processing system. Such an investment by Congress would be significant. However, it would quickly pay for itself.

Congress and the IRS could work with the petroleum industry to devise a reporting system which would, with a minimum burden to industry, maximize the Service's ability to identify tax fraud promptly. Such a system would enable the limited staff available to the IRS to target parties for enforcement action and terminate evasion schemes quickly. This type of enforcement is the only way to provide sufficient deterrence to ensure that evasion is minimized and that the Treasury collects the revenues which Congress intended.

SIGMA appreciates the opportunity to present its views. If the members of the Subcommitee or your staff have any questions, please do not hesitate to contact us.

Sincerely,

J. Keith Ausbrook

JEFFREY L. LEITER
J. KEITH AUSBROOK
Counsel to the Society of Independent
Gasoline Marketers of America

JLL/JKA:vw

MAR 0 7 1988

The Texas Shrimp Association
403 Vaughn Building Austin, Texas 78701
Tel. (512) 476-8446, 476-8447

March 3, 1988

The Honorable Charles Hatcher, Chairman
Subcommittee on Energy & Agriculture
Committee on Small Business
405 Cannon House Office Building
Washington, DC 20515-1002

Dear Mr. Chairman:

The Texas Shrimp Association is a harvester level association representing 300 Gulf shrimp vessels and 100 support corporations. Most of our members are based in Texas, but we do have members from other Gulf states as well.

We thank you for the opportunity to comment on H.R. 3865, the diesel fuel excise tax collection bill. We wholeheartedly support the bill. We believe that requiring fishing vessel operators to apply for a tax refund imposes a significant paperwork burden on these small businessmen. The refund process itself is an additional administrative nightmare for both the applicant and the Federal Government.

Many of our members operate on a narrow margin. They cannot afford for the Federal Government to be using their money and drawing interest upon it. These operators need that money for payment of their vessel mortgages, insurance premiums, vessel and gear repairs and replacement, as well as basic living expenses.

In the shrimp industry, fuel is the major cost of operating the vessel. It accounts for approximately 25 to 33% of operating expenses. An average Gulf shrimp vessel — 55 to 80 feet long — uses approximately 50,000 gallons of fuel in a year. In 1987, the average price of diesel fuel to the vessel was $0.62 per gallon. Approximately, $7,550 would be paid as an excise tax if the new law is enacted in April.

In Texas, we estimate that a total of $14.4 million would be totally or temporarily withheld from the economy on an annual basis if the current provisions are maintained.

We do not believe it is equitable to tie up a fisherman's $7,550 when he does not owe that money to the Government. Futhermore, the loss of $14.4 million for any period of time from our coastal economy would be devastating. We urge the Committee to favorably report out H.R. 3865.

Sincerely,

Ralph Rayburn

Ralph Rayburn
Executive Director

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